Global COVID-19 pandemic pulls service sector back into contraction

Key findings

Service sector output declines as global demand deteriorates...

...contrasting with growth at seven-year high in February

Firms cut employment as spare capacity emerges

Having recorded the strongest rise in business activity for over seven years in February, latest survey data brought this to an abrupt end as services output in India declined in March. According to firms, the outbreak of the coronavirus disease 2019 (COVID-19) dented client demand, particularly in overseas markets, as discretionary spending was knocked by public health measures aimed at stemming the outbreak.

Firms responded by reducing their workforces as intakes of new business were insufficient to maintain payroll numbers. That said, input costs rose at the slowest rate in six months as market prices for food and fuel were cut by suppliers.

The IHS Markit India Services Business Activity Index recorded 49.3 in March, down from February's 85-month high of 57.5. The headline figure fell by over 8 points, undoing the strong gains in growth momentum seen throughout 2019 so far. According to panel members, business activity was reduced in response to weaker demand. The global COVID-19 pandemic reportedly led a fall in new orders from clients, particularly overseas. That said, the decrease in output was mild overall. March data were collected between 12-27 March.

Latest survey data pointed to the first fall in order book volumes at Indian service providers since September 2019. Although the drop in demand was modest, it was the sharpest for just over two years. There were widespread reports of new business receipts struggling due to the COVID-19 outbreak, deterring discretionary spending. A number of firms also mentioned lower sales as a result of liquidity issues.

Poor conditions in overseas markets led to the sharpest deterioration in foreign demand since exports data were first collected in September 2014. The global COVID-19 pandemic had a far-reaching impact on the ability of firms to source new work intakes from abroad.

In response to reduced business requirements, the level of employment across the Indian services sector fell as firms cut workforce numbers to keep operating costs tight. That said, the rate of job shedding was mild as the large majority of firms (93%) left payroll counts unchanged.

There was nonetheless some evidence of capacity pressures being generated, albeit to a lesser degree. Backlogs of work rose at a slight, but weaker rate in March.

Looking further ahead, latest data showed firms were still optimistic that activity levels would rise over the next 12 months as the extreme measures to curb the spread of COVID-19 are lifted and global demand begins to recover. That said, the level of confidence dipped to a five-month low.

Lastly, input costs facing Indian service providers increased at the slowest rate for six months during March. Anecdotal evidence suggested that lower market prices for food and fuel contributed to a weaker rate of inflation. There were reports of suppliers cutting fees due to low demand. Consequently, output charges rose at a pace that was softer than in February and below its long-run average.

continued...
Private sector output growth slows to marginal pace in March

The Composite* PMI Output Index fell to 50.6 in March, down 7 points from February’s 57.6 to signal a sharp slowdown in private sector output growth and bringing an abrupt end to the recent strong upward-moving expansion trend. Overall, the index was consistent with a marginal rate of increase in private sector output.

The expansion was upheld by the manufacturing sector, which observed a solid rise in production volumes over the month. This contrasted with a shallow decline in services activity.

That said, overall new order intakes fell marginally in March as the fastest drop in demand for services for over two years pulled aggregate sales into negative territory.

Meanwhile, employment levels broadly stagnated across India’s private sector economy as slight growth in manufacturing was offset by a mild drop in staffing levels across the service sector.

Composite indices are weighted averages of comparable manufacturing and services indices. Weights reflect the relative size of the manufacturing and service sectors according to official GDP data. The India Composite Output Index is a weighted average of the Manufacturing Output Index and the Services Business Activity Index.

Comment

Commenting on the latest survey results, Joe Hayes, Economist at IHS Markit, said:

“The impact of the global COVID-19 pandemic on India’s services economy has not been fully realised yet. March PMI data showed business activity falling mildly. Crucially however, the survey data collection (12-27 March) was concluding just as Prime Minister Modi ordered a complete lockdown of the country.

“Strong growth momentum seen so far in 2019 was halted in March as demand conditions deteriorated, particularly overseas, leading to a reduction in business activity. Clearly the worse is yet to come as nationwide store closures and prohibition to leave the house will weigh heavily on the services economy, as has been seen elsewhere in the world. Pressure now fully lies on the government to combat the economic challenges the lockdown will cause.”
Survey methodology
The IHS Markit India 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
March data were collected 12-27 March 2020.

Survey data were first collected December 2005.

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