Services activity declines at substantial rate once again in May

Key findings

Global COVID-19 pandemic leads to further historic drop in output

Demand for Japanese services continues to fall sharply

Employment falls at sharpest rate since February 2010

Japan’s service sector remained under intense pressure during May, according to the latest PMI data, as business activity fell at a rate that before the coronavirus disease 2019 (COVID-19) pandemic was unparalleled in over 12 years of survey data. Demand for Japanese services fell considerably again in May amid further event cancellations and store closures.

Meanwhile, growing excess capacity led firms to cut employment at the fastest rate since February 2010, while business expectations remained inside negative territory for a third successive month.

The au Jibun Bank Japan Services PMI® is compiled by IHS Markit from survey responses from 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 headline figure is the Services Business Activity Index, which tracks changes in the volume of business activity compared with one month previously. A reading above 50 indicates an overall increase compared to the previous month, and below 50 an overall decrease.

The seasonally adjusted Japan Services Business Activity Index recorded 26.5 in May, still substantially below the 50.0 mark which separates contraction and growth, and therefore indicated a further decline in service sector output. Although the headline figure increased from April’s record low of 21.5, it remained indicative of a contraction in activity that was unparalleled in comparison to those seen since data were first collected in September 2007.

According to anecdotal evidence, store closures, cancelled events and weak sales contributed to the latest drop in activity. Over half of the survey panel registered lower output when compared to April, while just 6% of firms recorded growth.

Latest survey data pointed to a further sharp deterioration in demand conditions as a result of the global COVID-19 pandemic. While the reduction was slightly softer than seen in April, it remained unprecedented in scale. New export orders also fell drastically, although the rate of reduction was the weakest in three months.

Amid a further weakening in demand pressures, excess capacity continued to grow markedly at Japanese service providers. With business requirements falling, some companies reduced their workforces. Latest survey data pointed to the fastest decline in staffing levels since February 2010.

Looking ahead, surveyed companies retained a negative outlook on prospects for service sector activity over the next 12 months. According to panel members, the unpredictable nature of the COVID-19 pandemic underpinned caution among a number of firms. Some companies also anticipate that demand levels will be substantially weaker for the foreseeable future. However, the degree of pessimism was the weakest since February as some firms predict a resumption of business activity.

Lastly, price pressures remained deflationary during May as both input prices and output charges fell when compared with April. Anecdotal evidence suggested that both operating expenses and priced charged fell due to the impact of coronavirus.
au Jibun Bank Japan Composite PMI®

Economic activity plummets once again during May

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

The au Jibun Bank Japan Composite Output Index recorded 27.8 in May, substantially below the neutral 50.0 mark and thus indicative of a severe decline in combined output across both the manufacturing and service sector. The headline figure was only narrowly up from April’s record low (25.8) and therefore signalled a decline in output that was historically unparalleled prior to the COVID-19 pandemic.

By sector, trajectories diverged as a slightly weaker rate of contraction in services activity contrasted with a sharper fall in manufacturing output. However, in both cases, rates of decline were historically marked.

Meanwhile, private sector new orders fell substantially for a second month running, while employment was reduced at the fastest rate since September 2010.

Comment

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

"While the month of May has seen the Japanese government reduce the stringency of its lockdown, latest survey data indicated that economic activity continued to sink at a rate which had previously been unrivalled before the coronavirus crisis began.

"Services activity fell to a broadly similar extent to that seen in April as store closures continued and events were cancelled. Social distancing and reduced tourism are clearly having a severely negative impact on the service sector, and these factors are likely going to limit the speed and strength of any recovery as they continue over the short-to-medium term.

"Looking at May’s survey data in isolation, the reading of the Composite PMI is indicative of GDP falling by around 10% on an annual basis. Taking into consideration the April reading, which was even worse, it is clear that the impact on second quarter GDP is going to be enormous."
Methodology

The au Jibun Bank Japan 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.

May 2020 data were collected 12-26 May 2020.

About PMI

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