Service sector ends second quarter strongly, but outlook darkens

KEY FINDINGS

Business Activity Index ticks up to nine-month high of 55.8

Strong rate of job creation sustained... 

...despite weakest expectations for future activity since late-2015

Germany’s service sector ended the second quarter strongly, according to the latest PMI® survey, recording the fastest growth in business activity for nine months. Rising workloads, driven principally by stronger domestic demand, meanwhile helped sustain a robust rate of job creation.

However, the data showed growing concerns towards the outlook, with expectations for future activity falling to the lowest since late-2015.

June saw the headline seasonally adjusted IHS Markit Germany Services PMI Business Activity Index tick up to a nine-month high of 55.8, from 55.4 in May. The result completed the strongest quarterly growth performance since Q3 2014.

The upturn in business activity across the services economy remained broad-based by sub-sector. Leading growth was Post & Telecommunications, while Transport & Storage saw the weakest increase in activity.

Rising inflows of new work continued to form the basis for growth across the services economy. June saw new business increase at a solid rate that was quicker than that recorded in May, albeit slightly slower than April’s seven-month high.

Continuing the theme of recent months, the main driver of the increase in new business was stronger demand from domestic sources. New work from abroad fell for the eleventh time in the past 12 months and at the quickest rate since January 2015. Surveyed firms partly attributed this to delayed decision-making among European clients.

Service providers meanwhile reported sustained pressure on staffing capacity due to the rise in workloads, with backlogs of work increasing for a fifth straight month in June. Accordingly, a strong rate of employment growth was maintained, albeit with job numbers rising the least since March. Sub-sector data showed payroll numbers increasing across all monitored segments.

Higher average labour costs, alongside increased fuel prices, drove an overall rise in operating expenses across the service sector in June. The rate of inflation was elevated in the context of the survey history (since 1997), but eased since May to the second-lowest in over a year.

A backdrop of robust underlying demand and rising cost burdens led service providers to raise output charges in June. The rate of inflation accelerated from May’s 17-month low and was strong overall, though still comfortably below the highs seen towards the start of the year.

Finally, latest data indicated a softening of service providers’ optimism towards the year-ahead outlook for business activity. Sentiment weakened for the fourth month in a row in June to the lowest overall since October 2015. A number of firms highlighted concerns towards a slowdown in the economy, while there were also mentions of worries about the autos sector and an ongoing demographic shift.
IHS MARKIT GERMANY COMPOSITE PMI®

June's Composite PMI signals further moderate output growth

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 Composite Output Index was unchanged at 52.6 in June, pointing to the continuation of a moderate rate of growth of German private sector business activity. In line with the trend in previous months, another strong increase in services activity offset an ongoing decline in manufacturing output.

Total new business meanwhile returned to growth in June, rising the most since November last year, albeit only modestly overall. The expansion was centred on the service sector, where stronger demand from domestic clients countered weaker inflows of new work from abroad. With manufacturers also recording lower international sales, total export business fell markedly again.

Employment growth remained close to May’s three-year low at the end of the second quarter. That said, despite further cutbacks across manufacturing, the overall pace of job creation remained above the long-run average.

A faster fall in manufacturing input prices in June helped weigh on overall cost inflation, which reached its lowest since August 2016. Output prices meanwhile increased at a rate that was unchanged from May’s 22-month low. Whereas services charges rose more quickly in June, manufacturing factory gate prices were unchanged, falling to rise for the first time in almost three years.

Finally, data showed a softening of future output expectations to the second-weakest since late-2014, reflecting reduced optimism among services firms.

COMMENT

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

“The services PMI data are quite a mixed bag. On the one hand, the indicators of current performance point to a very healthy situation, with business activity and employment continuing to rise strongly on the back of robust underlying demand from the domestic market.

“But the survey’s forward-looking indicator – the only one based on sentiment – raises question marks over how long the service sector can continue growing at such a pace and keep compensating for the weakness in manufacturing. Slowdown fears have weighed on service sector optimism, which is now the lowest since October 2015.

“Overall employment in Germany is now in a lower growth phase, with the service sector providing the bulk of new jobs. In a similar vein, the PMI data have shown the strongest quarterly growth performance from the service sector for almost five years, but thanks to falling manufacturing production, overall economic output looks to be expanding at only a moderate pace.”
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.

June 2019 data were collected 12-25 June 2019.