Services Landscape

21 January 2020

Hang On A Minute

As the New Year gets underway, there seems to be some hope building that the economy will do better in 2020 than it did in 2019. Various business confidence surveys have shown a little less pessimism recently. And, so the story goes, the hard data will start to show improvement before too long. If that is the story, the script did not get to the Performance of Services Index respondents in December. Maybe it was lost in the Christmas mail. Whatever the case, the PSI was undeniably weak in December, slipping further to 51.9 from November's already below-average 52.9. This is the lowest PSI reading since September 2012 and has occurred despite a strong underpinning from buoyant population growth. The sales index has slipped to 52.6 from 53.9 in November.

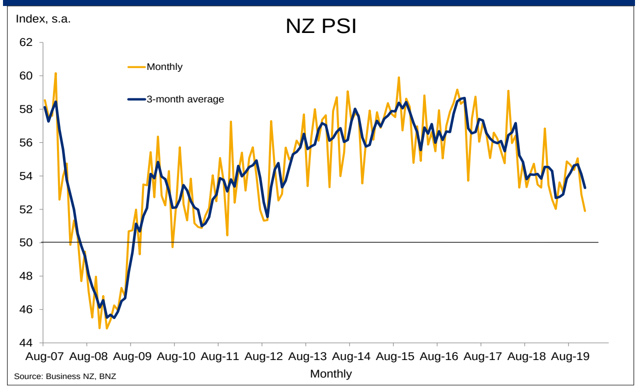
Signal or Noise?

At this point, it is difficult to determine if the PSI dip is a signal of more weakness ahead or rather a result of the material uncertainty prevailing through the latter part of last year. We say this as December's economic data is notoriously tricky to decipher signal from noise with various holidays and trading day changes occurring. By the same token, it would be remiss to dismiss this out of hand. In the least, it will sharpen focus on the coming month's data. Employment was a rare positive within the December PSI. It inched up to 52.3 from 51.6. The mix of weak sales yet solid employment raises the possibility that the sales weakness could prove temporary. Firms wouldn't be employing more staff if they thought sales were going to remain weak. New orders did edge a touch higher in December but, at 54.5, are still well below average. It's helpful that inventory looks to be under control after an odd looking spike in November.

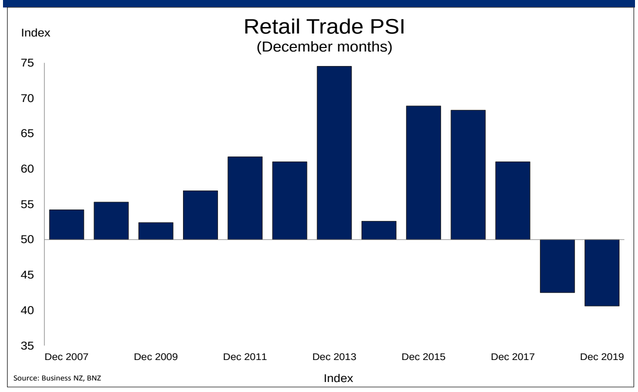
Grounds For Hope

With the housing market warming up again, an important consideration for the service sector – and the economy as a whole – this year is how much it encourages household spending. Evidence to date is mixed with fits and starts in the likes of the electronic cards transactions data through November and December. For the PSI, at least to date, the indications are unambiguously weak. Indeed very weak, if judged by the retail industry posting its lowest December since the survey started back in 2007. To be sure, this might reflect a change in festive purchasing patterns as much as anything else (with the likes of Singles Day and Black Friday sales seeing spending brought forward). It may also reflect industry challenges such as offshore competition and rising costs rather than a lack of overall sales per se. But, to us, the degree of retail PSI weakness in December suggests it shouldn't be ignored. Those looking for evidence of a strong, broad-based, pick up in spending on the back of a firming housing market will need to look elsewhere, or, in the least, need to wait a bit longer. Already signalled fiscal stimulus has the potential to lift demand ahead. Architects, responding to the latest Quarterly Survey of Business Opinion, have become more optimistic about the way ahead particularly with respect to government-led work. This bodes well for more service sector activity. Putting all this together, these factors offer hope for improvement in 2020. But December's PSI unequivocally counsels caution for the time being. Indeed, combining the weak PSI with last week's retreat in the PMI suggests the economy may be currently travelling at a sub-2% rate. It certainly questions those thinking that the economy can grow at 3% this year. Our forecast remains around 2%.

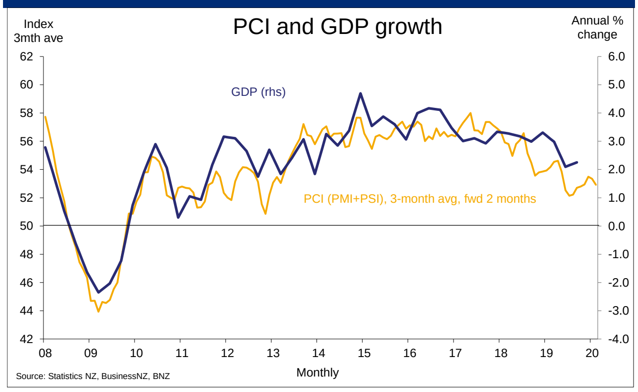
Deceleration



Weak Retail



Run Rate Sub 2%



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