Research

Services Landscape

18 September 2023

No respite

August brought no respite for the service sector. After dropping to 48.0 in July, the Performance of Services Index (PSI) slipped further below breakeven to 47.1. The trend remains downward. It is always difficult to be sure what exactly drives change in the PSI. But to the extent that things like very strong net immigration, some recovery in house prices, and the FIFA Women’s World Cup have supported service sector activity, it suggests a sizeable scale of underlying weakness emanating from other factors. We’d surmise the impact of the high cost of living, high interest rates, and weaker export prices have dented aggregate activity. Some election uncertainty could also be at play. The PSI activity/sales (43.4) and new orders (47.3) components both posted their second consecutive month well below 50, albeit both were less negative than in July.

More recessionary than not

The weakening PSI looks like the PMI from last week. The combined PCI index slipped to average 47.0 in August, from 47.8 in July. This adds to the notion that economic growth struggled into the second half of the year. That is worth bearing in mind as this week’s GDP figures for Q2 shape to post a reasonable bounce. The latest PCI readings suggest any such bounce will be short lived and are consistent with economic contraction returning. In this sense, the PMI and PSI results are more consistent with the RBNZ forecast of a return to recession than the Treasury’s latest forecasts of moderate growth ahead.

Rebalancing

From an RBNZ policy perspective, the balance of supply and demand is more important than growth itself. A negative gap has recently opened between the PCI demand indicators like sales and new orders and PCI supply indicators like employment, inventories, and supplies. This suggests that the extent to which demand is outpacing supply is easing. For example, PCI new orders (averaged 47.4 in August) are relatively weak compared to PCI inventories that continued to expand (at an above average 52.0 in August). Interestingly, PSI employment rose to 50.9 in August, from 49.1 in July. This lift may well reflect more labour supply via migration as it does any underlying increase in labour demand. In any case, it shows another month where the PSI employment indicator has come in above sales and new orders. The glass-half-full interpretation of this is that it shows supply side expansion that will help take the heat out of inflation. On the other hand, it is not a good look for labour productivity.

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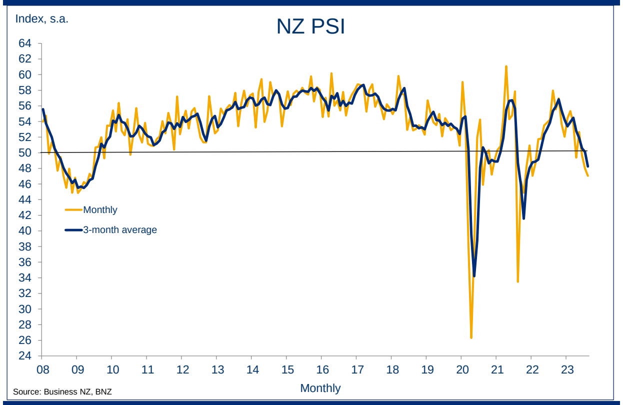
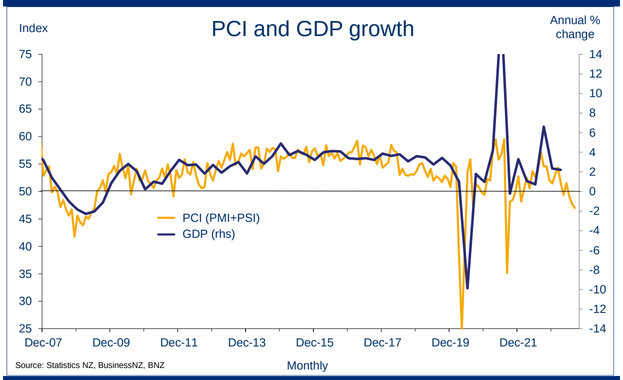
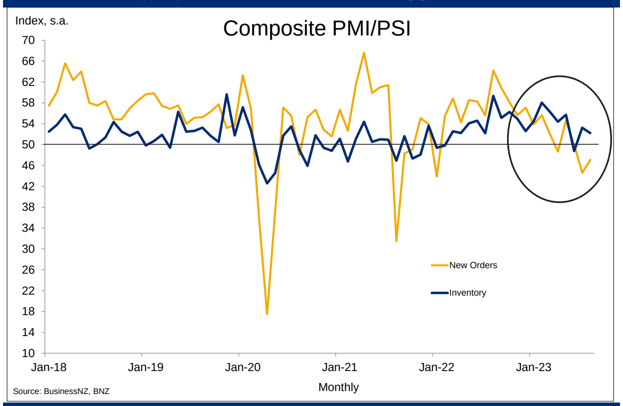
Service Still Sliding



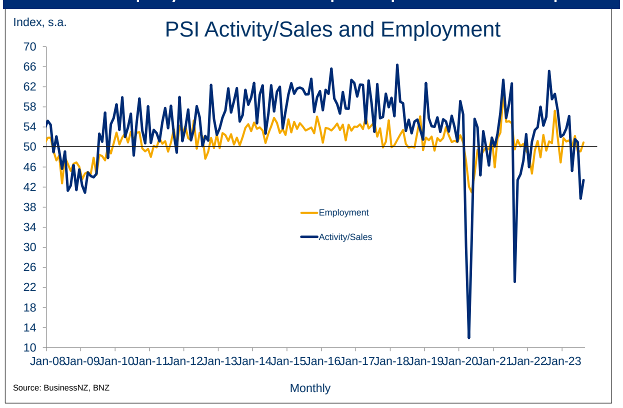
Poor Growth Signal



PCI Inventory Up as New Orders Struggle



Services Employment Holds Up Despite Sales Slump



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