

## UK service sector slows further as Brexit uncertainty builds

With Brexit uncertainty causing investment to decline, service sector activity has slowed as new orders become scarce. A lot will hinge on the events today in Westminster, but the bottom line is that risk of a 'no deal' Brexit on 31 October is unlikely to fade completely after this week. This will continue to keep the pressure on underlying growth



Source: iStock

At 50.6, the latest UK services PMI suggests that the sector is barely growing. With the exception of the July 2016 dip, business optimism is now at the lowest level seen since the financial crisis. So what does this mean for growth?

Well, IHS/Markit note that these PMI levels are usually consistent with a fall in output of -0.1% during the third quarter. Given the prospect of further volatility in the inventory numbers, this seems unlikely at this stage – we may see firms build stocks again ahead of the 31 October deadline, albeit at a slower pace than back in the first quarter (inventory levels are still reasonably high). This recorded as a positive for economic output, although of course is ultimately a temporary phenomenon.

---

*IHS/Markit note that these PMI levels are usually consistent with a*

## *fall in output of -0.1% during the third quarter*

---

However, there's little doubt that the underlying pace of growth is likely to stay fairly lacklustre. Investment has been more-or-less consistently declining since the start of 2018, and this is a trend that is likely to persist. While the outcome of the coming 24-hours will be critical for the Brexit process, it seems unlikely at this stage that this week's events will fully take the 'no deal' risk off the table.

This uncertainty will continue to limit appetite to expand, and as firms continue to ramp up contingency activities in the run-up to the October deadline, resources available for possible investment projects will also be diminished.

For the services sector, this lower investment trend has reduced demand for the associated professional/financial services, according to the Bank of England analysis last month. The pace of new orders has slowed and firms are reporting that backlogs of work are falling. With wage and other input prices rising, IHS/Markit note that this is putting "intense" pressure on margins as firms don't have the power to pass these costs on. In turn, this suggests risks to hiring and capital spending within the sector over the coming months.

The upshot is that underlying growth is likely to remain fairly lacklustre over coming months. That said, barring a 'no deal' exit in October, we think it's still too early to be pencilling in UK rate cuts over coming months. Equally however, the prospect of further gradual tightening is becoming increasingly distant.

### Author

#### James Smith

Developed Markets Economist, UK

[james.smith@ing.com](mailto:james.smith@ing.com)

### Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial

Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.