UK services PMI offers faint glimmer of hope for BoE

There's little doubt the service sector is continuing to struggle as Brexit uncertainty comes to the fore once again. We don't expect a rate hike from the Bank of England this year, but with the latest services PMI hinting at stronger hiring demand and some core inflationary pressure, there are some glimmers of hope for policymakers

Source: iStockphoto

At 51, the latest Markit/CIPS PMI is a touch better than in April, but nevertheless suggests the uncertain backdrop is continuing to weigh on growth.

Beneath the headline figures though, we think there are two glimmers of light for the Bank of England.

51.0 UK services PMI (May)

Better than expected

1 Stronger job creation

Firstly, Markit/CIPS noted that the rate of job creation was the strongest for six months. On one hand, this could be a continuation of a recent trend whereby some firms appeared to increase hiring to offset lower investment, on the basis that staffing levels are easier to change in future given the uncertainty surrounding Brexit.

However, the press release noted that in this case, the hiring flurry was linked to “long-term business expansion” and “efforts to boost operating capacity”. It therefore seems more likely that the Article 50 extension and corresponding temporary dip in uncertainty has, at least to a certain extent, helped unlocked some pent-up demand for labour.

2 Firms passing on higher wage costs to customers

The other ray of hope for the Bank of England stems from costs. As has been the case for some time, the report indicates that wage costs are rising (partly linked to the tight jobs market, but also the marked increase in the minimum wage over recent years). The key thing as far as policymakers are concerned is that stronger levels of demand, coupled with “efforts to protect margins”, are prompting firms to pass these higher costs onto the consumer.

Given that wage growth has been a key pillar of the Bank of England’s argument for further tightening, this latter point suggests that a rate hike later this year shouldn’t be 100% ruled out. Don't forget that Governor Mark Carney hinted back in May that markets are underestimating the central bank's tightening plans.

In reality though, we think it is much more likely that the Bank keeps policy unchanged for the rest of 2019. While the recent, weaker PMIs don't completely tally with the more resilient 'hard data', this latest subdued survey reading suggests that growth is likely to remain fairly lacklustre over coming months. With ‘no deal’ fears rising once again, we expect investment to continue falling, offsetting some marginally better news in consumer spending.

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