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PRESS RELEASE

NUMBER OF SECTORS REPORTING FALLING OUTPUT DOUBLES AMID SLOWING DEMAND

- Output fell in six out of 14 UK sectors in May, compared to three in April
- Eight sectors continue to see output growth, though down from 11 in April
- Number of sectors reporting a fall in new orders reaches highest since January 2021
- Service sector firms bear the brunt of cost inflation and strongest margin pressures
- Technology manufacturers buck wider trend with fastest output growth of any sector
- Input prices reach record high, but firms continue to hold back from fully passing on costs

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The number of UK sectors reporting a fall in output doubled in May, as inflation continued to drive down demand for goods and services, according to the latest Lloyds Bank UK Sector Tracker.

Six out of the 14 sectors monitored by the Tracker saw overall output contract, compared to three in April. This was the largest number reporting a fall in output since February 2021. However, eight sectors still saw output growth, down from 11 in April, albeit five sectors showed a slower rate of month-on-month growth.

The slowdown was driven by falling demand, as consumers and businesses reined in spending amid record levels of inflation. Eight out of the 14 sectors monitored experienced a fall in new orders in May – the highest number since January 2021.

In response to this, it is expected that businesses will focus on balancing their levels of stocks, and to ensure they have sufficient raw materials ahead of any further price rises, but avoid having too much working capital tied up, restricting investments elsewhere.

Household product manufacturers registered the fastest decline in output of all 14 sectors monitored by the Tracker in May (45.6 in May vs. 48.5). This sector also reported report a steeper contraction in new orders (45.5 in May vs. 48.6 in April) amid the ongoing consumer shift, post-lockdowns, towards spending on recreational activities, and more restrained consumer spending.

Meanwhile, food and drink producers saw output contract for the first time since July 2021 (47.5) as new order levels also fell (49.2 in May vs. 53.3 in April). Firms attributed weakened demand to a slowdown in client stockpiling amid sharply rising prices.

However, manufacturers of technology equipment bucked the wider trend in May. Firms posted the fastest rate of output growth (68.0) of any sector, citing strong demand from businesses investing in their own operations.

The UK Sector Tracker is an evolution of the Lloyds Bank UK Recovery Tracker. It uses PMI data from S&P Global to shed light on current trends in the UK economy. A reading above 50 on the Tracker indicates expansion on an index, while a reading below 50 indicates contraction.

Cost inflation hits new record high in services, as firms hold back on raising prices

Firms across the UK faced significant price pressures in May. The Tracker's composite Input Prices Index reached a record high (85.9) – exceeding the previous record set in April (83.5) and well above the 10-year average reading of 60.0.

The rise in cost inflation was driven by the service sector, which saw input costs rise at a record rate (85.8), as businesses continued to grapple with higher energy bills and wage costs amid fierce competition for staff.

For the second month, cost inflation was highest among tourism and recreation firms, which includes pubs, hotels, restaurants, and leisure facilities. Firms here posted 93.3 on the Tracker's Input Cost Index, driven by higher operating costs and recruitment challenges.

As input prices have risen, businesses have continued to hold back from fully passing on costs to customers. Moreover, the gap between the Tracker's composite Input Price Index (85.9) and the composite Prices Charged Index (69.2) grew month-on-month to (16.7) index points (vs. 14.1 in April).

The difference between the Input Price and Output Price Indices was greater amongst service businesses (17.8) than manufacturers (10.2), suggesting more intense margin pressures amongst service sector firms.

Jeavon Lolay, Head of Economics and Market Insight at Lloyds Bank Commercial Banking, said: "High inflation is dampening consumer demand and increasingly weighing on the ability of companies to pass on rising costs. Our latest UK Sector Tracker shows service businesses having their margins squeezed more tightly than manufacturers.

"Recently, the gap between input costs and prices charged was widest for manufacturers, primarily reflecting the impact of the pandemic on international supply chains and stronger relative consumer demand for goods than services. The reversal of this trend evidences both changing spending habits and that service providers are becoming more concerned about the potential fragility of customer demand. However, the broadening of price pressures across the economy also points to the risk of more persistent inflation and therefore more policy tightening by the Bank of England.

"All eyes will remain fixed on forthcoming UK activity and inflation data to assess the potential scale, pace and timing of further rate increases from the Bank of England."

Scott Barton, Managing Director, Corporate and Institutional Coverage, Lloyds Bank Commercial Banking, said: "Continued input cost inflation means it's more important than ever for businesses to ensure they have a healthy cashflow.

"With inflation at its highest point in 30 years, firms may face larger up-front operational costs than they have before, and a larger working capital requirement.

"Any excess funds tied up in unused inventory, unsold stock or elements like unpaid invoices are funds that can't be used to seize on new opportunities, wherever they arise. Optimising their finances will help ensure firms have the maximum possible liquidity to help them be flexible in their operations and trading and to continue where possible to pursue their growth objectives."

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Notes to Editors

The UK Sector Tracker (UKST) is an evolution of the Lloyds Bank UK Recovery Tracker. It uses PMI data from S&P Global to shed light on current trends in the UK economy.

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The UKST builds on the core data set of the UK Recovery Tracker – evolving to deliver deep insight into the topics and themes most relevant to today's economic environment as UK GDP returns to pre-pandemic levels.

Methodology

The Lloyds Bank UK Sector Tracker includes indices compiled from responses to S&P Global's UK manufacturing, services and construction PMI® survey panels, covering over 1,500 private sector companies.

The report also features S&P Global Sector PMI indices, which are compiled by S&P Global from responses to questionnaires sent to purchasing managers in S&P Global's global PMI survey panels, covering over 27,000 private sector companies in more than 40 countries.

S&P Global maps individual company responses to industry sectors according to standard industry classification (SIC) codes, covering the basic materials, consumer goods, consumer services, financials, healthcare, industrials and technology sectors across varying tiers of detail.

The Lloyds Bank UK Sector Tracker monitors the following 14 individual UK and Global sectors: Chemicals, Metals & Mining, Automobile & Auto Parts, Beverages & Food, Household Products, Tourism & Recreation, Banks, Real Estate, Healthcare, Industrial Goods, Industrial Services, Transportation, Technology Equipment, Software & Services.

In April, the UK sectors recording output growth were: Chemicals, Metals & Mining, Automobiles & Auto Parts, Tourism & Recreation, Healthcare, Industrial Goods, Industrial Services and Technology Equipment.

In March, the UK sectors recording faster output growth month-on-month were: Metals & Mining, Healthcare, Transportation and Technology Equipment.

Survey responses are collected in the second half of each month and indicate the direction of change compared to the previous month. Global survey responses are weighted by country of origin, based on sectoral gross value added. 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 Purchasing Managers' Index (PMI) survey methodology has developed an outstanding reputation for providing the most up-to-date possible indication of what is really happening in the private sector economy by tracking variables such as sales, employment, inventories and prices. The indices are widely used by businesses, governments and economic analysts in financial institutions to help better understand business conditions and guide corporate and investment strategy. In particular, central banks in many countries use the data to help make interest rate decisions. PMI surveys are the first indicators of economic conditions published each month and are therefore available well ahead of comparable data produced by government bodies.

For further information on the PMI survey methodology, please economics@ihsmarkit.com

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