

14 June 2021



Strong expansion

Service sector expansion remains strong. The Performance of Service Index (PSI) headline reading of 56.1 in May portrays strength. Sure, it didn't match April's record high of 61.2, but it is still well above its long-term average of 53.8, indicating above average growth. New orders, at 62.1 in May, continue to be the strongest of the PSI's sub-components indicating buoyant demand conditions. It appears the overall PSI would be even higher were it not for significant issues on the supply side.

With challenges

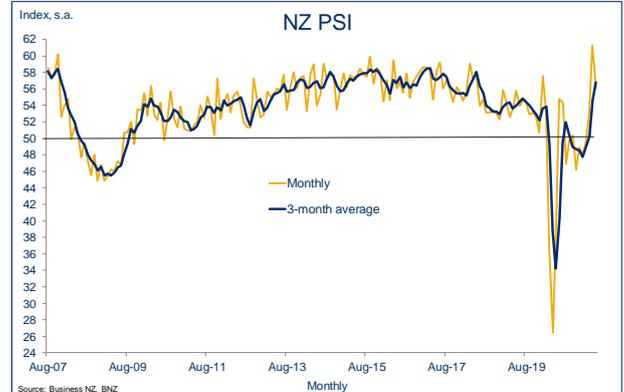
Amid the broad positive tenor of the PSI, the service sector is not without significant challenges. First, the general lack of international tourism and education continues to see acute pain in parts, even if the trans-Tasman bubble has helped some at the margin. Second, supply side issues are pervasive and persistent. This is evident in the PSI's supplier deliveries component. After a hint of becoming less negative in April, it dipped again in May to 45.1. That makes 10 consecutive months of being below the 50 line that delineates between positive and negative. Beyond the numbers, many survey respondents note issues with the likes of availability of inputs, higher shipping costs, freight delays, supply chain distortions, and cost increases. Flooding in the South Island late in the month caused its own set of issues. Difficulty finding appropriate labour was widely reported in various ways. That suggests that the above average PSI employment index of 54.3 in May would have been even higher had it not been for supply constraints. As it is and combined with a solid employment reading in last week's PMI, it firmly supports our view that the unemployment rate will continue to fall.

Demand pressuring supply

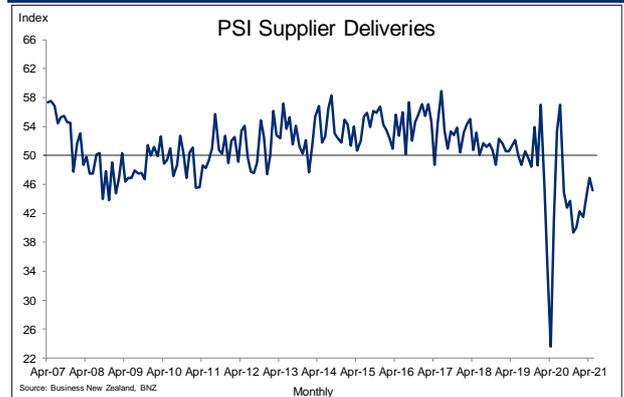
In contrast to the considerable difficulties on the supply side, demand looks vigorous. Combining PSI new orders and sales as an indicator of demand gives a May average of 60.4. That far exceeds the combination of PSI employment, inventories, and supplier deliveries which averaged 50.3 in the month. Importantly, the gap between the two is nearly double its long-term average highlighting the current pressures on the capacity of firms to delivery what is being required of them. While the current strength in the PSI (and PMI) says good things for economic growth over coming quarters, the obvious supply side stresses suggests significant upward pressure is building on inflation. Annual CPI inflation is expected to rise aggressively, starting with Q2 figures due next month.

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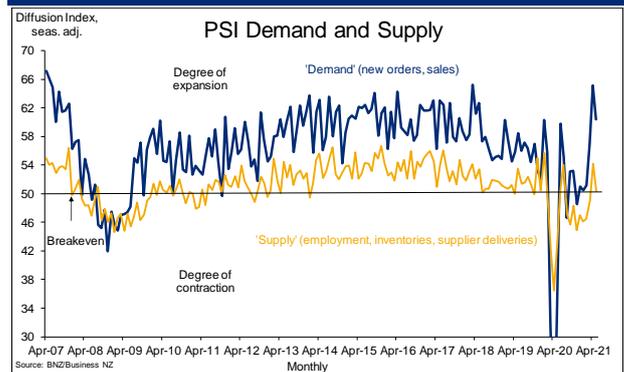
Buoyant



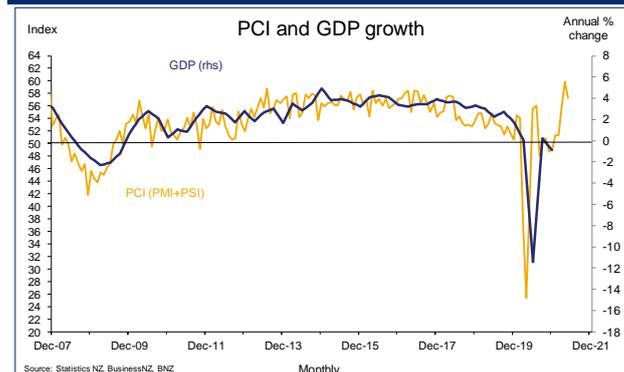
But Not Without Difficulties Here



Imbalance



GDP To Lift



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