

Australian Chamber–Westpac Survey of Industrial Trends

Australian Chamber of Commerce and Industry & Westpac Banking Corporation

225th report December 2017 (survey conducted 13th November to 4th December 2017)

- The Australian Chamber-Westpac Survey of Industrial trends, Australia's longest running business survey dating from 1966, provides a timely update on manufacturing and insights into economy-wide trends.
- The Westpac-AusChamber Actual Composite index fell in December 2017, down to 63.4 from 66.1 in September. That is a slight pull back after an extended rebound from 55.1 in June 2016, a dip coinciding with the July Federal election.
- The above par reading for the Composite Index, which has trended higher since 2014, reflects strength in new orders, output, overtime, backlog and employment. While the momentum in new orders, output and backlog moderated, employment remained robust.
- Manufacturing is benefitting from: a strong upswing in public infrastructure investment; renewed expansion in non-mining business investment; and a still relatively low Australian dollar combined with a lift in global growth. The level of home building activity is still high, but it is now turning lower. More pressing negatives are: subdued consumer spending constrained by slow wage growth; and continuing intensity from offshore competitors.
- The uptrend in exports has continued at a moderate pace after stumbling in 2016, with a net 4% of firms indicating a rise in export deliveries. Export expectations are moderately positive, coinciding with rising world trade volumes after a period of contraction as well as support from a relatively low AUD.
- Expectations are positive, centred on new orders and output as well as backlog and overtime. The Expected Composite is at 61.8 in December, down from 65.2 in September and 65.7 in June. A net 29% expect the general business situation to strengthen over the next six months. While lower than the past quarter, the survey result continues to reflect an upbeat mood.
- Equipment investment intentions of respondents have been positive over recent years in response to rising demand and consistent with a reduction in the sector's spare capacity, as well as improving profitability. A net 15% of firms expect to increase equipment investment in the next year. Building intentions have recovered to a net 2% in December after dipping to a net -3% in September.
- The survey's Labour Market Composite, which broadly tracks economy-wide jobs growth, is at 60.0 in December, pointing to continued solid jobs growth in the near-term. The index correctly foreshadowed the acceleration in Australian employment through 2017.

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Net response or "balance" is calculated by the proportion of "ups" less "downs" on individual questions, thereby yielding the net balance.

A positive balance indicates a net upward or improving trend and a minus balance a net downward or deteriorating trend.

The 225th consecutive survey was closed on 4 December 2017.

A total of **264** responses were received, and provided a reasonable cross-section of Australian manufacturing in respect of industry groups and size of operation.

The next survey will be conducted over February/March 2018.

Key survey results

Westpac–AusChamber Composites *(seasonally adjusted)*

	Q3 2017	Q4 2017
Actual – composite index	66.1	63.4
Expected – composite index	65.2	61.8

- The Westpac-AusChamber Actual Composite Index fell to 63.4 in December from 66.1 in September. However, this follows five consecutive increases and the Composite continues to be positive.
- Strength in the composite is underpinned by solid output, backlog and new orders, while employment and overtime is expanding.
- The robust level of December's result reflects increased investment in both state infrastructure projects as well as private non-mining construction. A relatively low AUD is also supporting exporters.
- The Expected Composite dropped to 61.8 from 65.2, down off June's 65.7. The cresting in home building is weighing on some firms in the manufacturing sector.

Westpac–AusChamber Labour Market Composite

	Q3 2017	Q4 2017
Net balance	60.1	60.0

- The survey provides insights into economy wide employment growth. This highlights the key linkages between manufacturing and the labour market.
- The Westpac-AusChamber Labour Market Composite was broadly stable at 60.0 in December compared to 60.1 in September.
- The index correctly led the uplift in employment through 2017 and the current high level of the Composite suggests that momentum should continue in the near term.
- Official employment data has shown robust jobs growth. In the year to October, the economy has added 356k jobs, +3.0%.

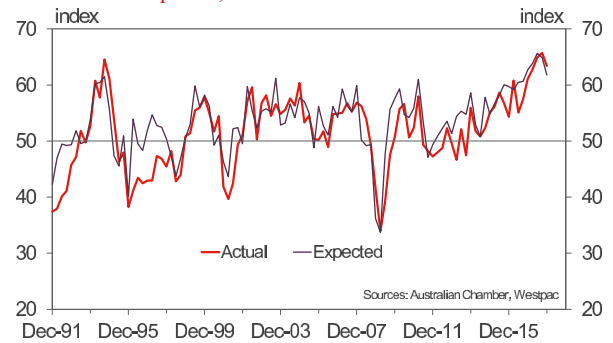
General business situation

	Q3 2017	Q4 2017
Net balance	35	29

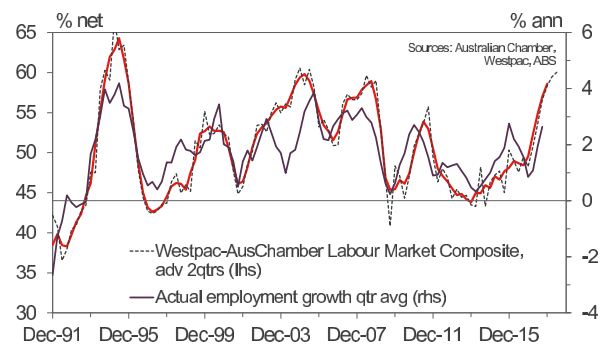
- Manufacturing firms are upbeat on the general business situation heading into 2018. A net 29% of respondents in December expect the business environment to improve over the next six months.
- The result is broadly consistent with the view over the past year - a net 37% in March, a net 28% in June, and a net 35% in September. Yet, December's drop does coincide with a moderation in the Expected Composite.
- The positive outlook of manufacturers is in line with the general business sentiment in Australia and around the world. The optimism corresponds with an uplift in world growth and trade.

Westpac-AusChamber Composite indexes

Actual & expected, sa

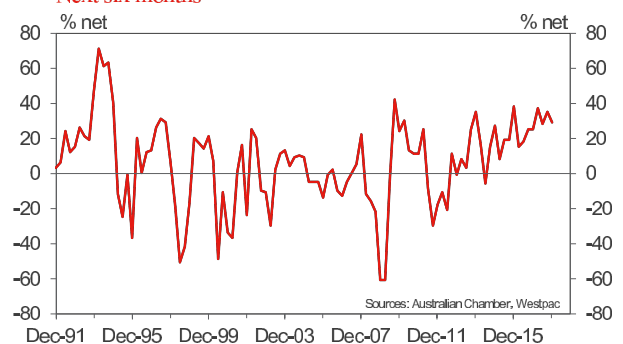


Employment: momentum picking up over 2017



General business situation

Next six months



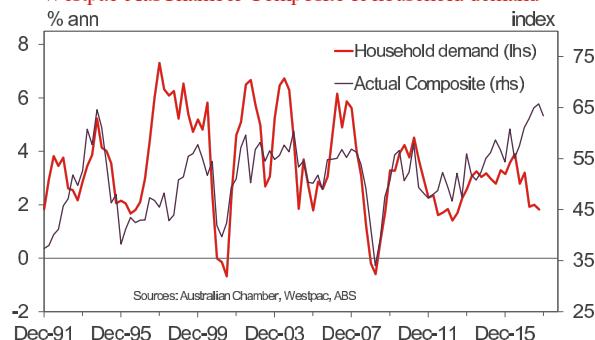
The business cycle & economic outlook

Manufacturing & the business cycle

- The Westpac-AusChamber Actual Composite Index has a solid track record of predicting near-term domestic economic conditions, identifying turning points in the cycle.
- The Composite generally tracks household demand. More recently, forces outside of households have been more significant in lifting manufacturing activity.
- Higher public and private business investment is seeing increased non-residential construction. The relatively low AUD and foreign demand is supporting exporters, particularly in food and beverages.
- The Actual Composite Index points to the economy achieving solid growth in the near-term, though the home building upswing has turned.
- In part, the index is elevated relative to actual activity due to the compositional effect of exiting firms.

Manufacturing & the business cycle

Westpac-AusChamber Composite & household demand

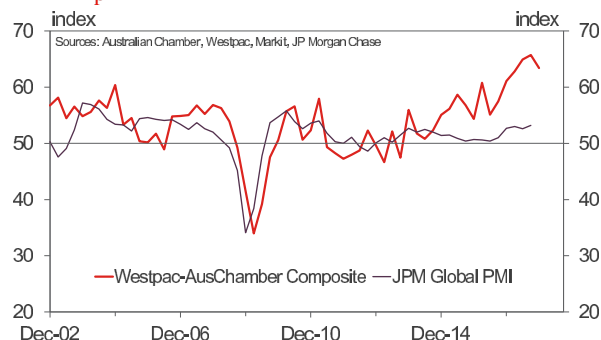


Australian & World manufacturing surveys

- Global and Australian manufacturing cycles tend to be synchronised, particularly at major turning points.
- Historically, the Westpac-AusChamber Actual Composite had moved broadly in line with global manufacturing indices.
- However, since 2014, the Composite has deviated to the upside. Partly this reflects Australian manufacturing outperformance as easier monetary policy triggered an upswing in home building activity, but also the transitional issue of exiting firms.
- Global manufacturing conditions have strengthened through 2017 after beginning to turn up late in 2016. That is in line with increased world trade volumes and stronger growth. Manufacturing sentiment is positive leading into 2018.

Australian & World manufacturing surveys

Westpac-AusChamber & Global PMI indexes

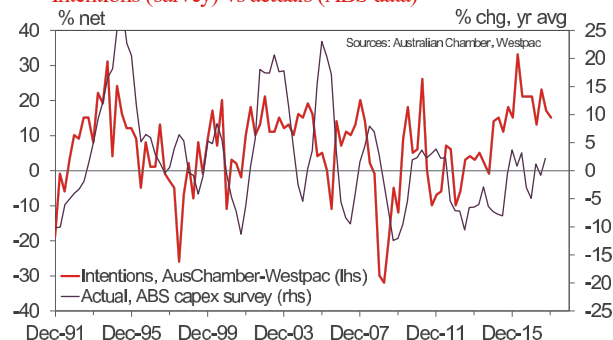


Manufacturing & business investment

- The AusChamber-Westpac survey has a solid record of predicting equipment investment by the manufacturing sector.
- Manufacturing firms are looking to invest in the year ahead. A net 15% of respondents expect to increase plant and equipment investment in the next twelve months.
- The ABS capex survey confirms that real manufacturing equipment investment is expanding. After a strong uplift in 2015/16, equipment investment consolidated in 2016/17 possibly in association with the July Federal election. The 2017/18 year started well and year average real manufacturing equipment investment is currently tracking at 3.3%.

Manufacturing equipment investment

Intentions (survey) vs actuals (ABS data)



Activity & orders

Output *(seasonally adjusted)*

	Q3 2017	Q4 2017
Actual - net balance	41	29
Expected - net balance	36	26

- Manufacturing output has expanded for fourteen consecutive quarters.
- The uptrend emerged in the second half of 2014 with momentum gradually gaining pace. However, December's result showed a lesser net 29% of firms increasing output compared to a net 41% in September.
- Expectations also dipped with a net 26% of respondents anticipating output to lift in the next three months. That is the second consecutive drop, with September a net 36% and June a net 40%.

New orders *(seasonally adjusted)*

	Q3 2017	Q4 2017
Actual - net balance	39	32
Expected - net balance	38	33

- New orders expansion has underpinned the lift in output, it too having increased in each of the last fourteen quarters.
- In December, a net 32% of respondents indicated higher new orders compared to a net 39% in September.
- A similar experience of volatility in new orders and output was seen in 2015 when the housing market cooled on tighter lending standards. The current period of tightening in 2017 has seen home building cresting.
- However, December's result is still very positive and well above average with non-residential construction supporting demand for manufacturing.

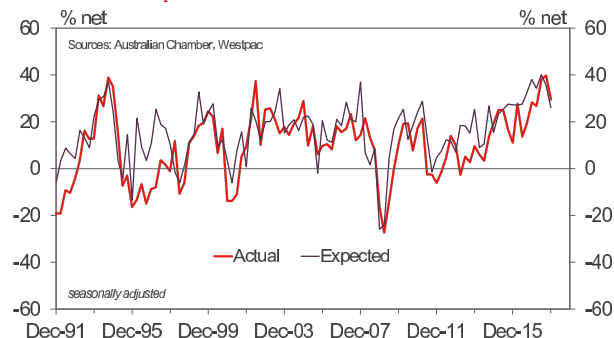
Exports

	Q3 2017	Q4 2017
Actual - net balance	8	4
Expected - net balance	4	3

- Exports continued to expand in the December quarter but a lower proportion of respondents reported higher exports. A net 4% of firms indicated that exports increased in December compared to a net 8% in September and a net 12% in June.
- Supported by a lower AUD following the mining boom, exports rose consistently through mid 2013 to early 2016. However, in June 2016, exports reported a brief dip with a net 3% of respondents indicating lower exports.
- Following this, exports have been in an uptrend, corresponding with stronger world trade. The recent slowing in momentum may be associated with an uptick in the AUD, which has since reversed.

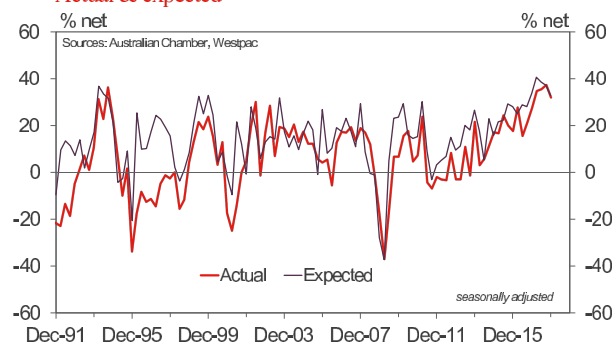
Output growth

Actual & expected



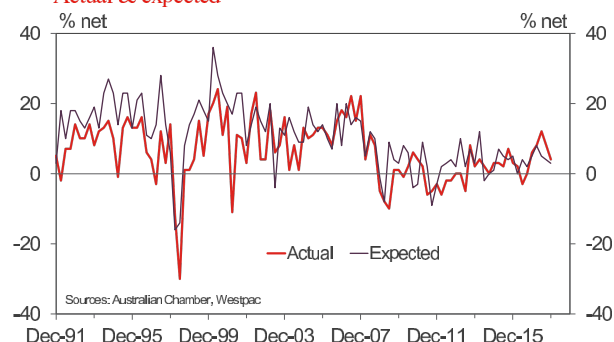
New orders

Actual & expected



Export deliveries

Actual & expected



Investment & profitability

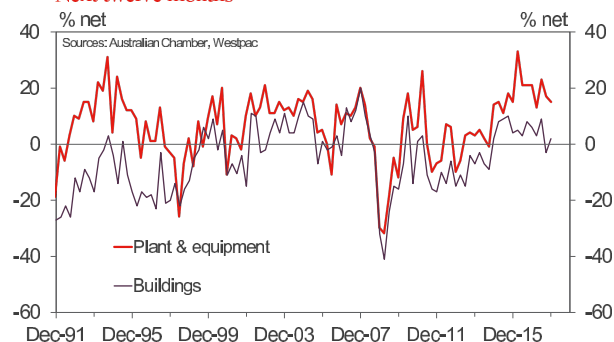
Investment intentions

	Q3 2017	Q4 2017
Plant & Equipment – net balance	17	15
Building – net balance	-3	2

- The survey, as it has since late 2014, indicates that manufacturing firms are planning to increase equipment investment to meet rising demand.
- A net 15% of firms indicated that they are intending to increase equipment investment over the next twelve months, broadly in line with the results from the last six quarters.
- Building investment intentions are back to being positive after posting a negative in September. In December, a net 2% of respondents expect to increase investment over the next twelve months.

Investment intentions

Next twelve months

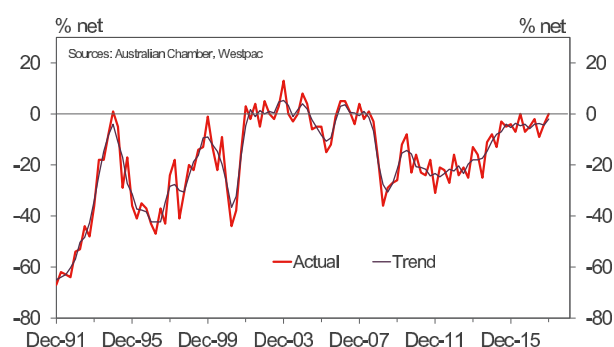


Capacity utilisation

	Q3 2017	Q4 2017
Net balance	-4	0

- Capacity utilisation levels have moved higher through 2017 after a pause following a strong uplift beginning in late 2013.
- The number of respondents operating above capacity was equal to those operating below capacity in December. This is stronger than September's net -4% and June's net -9%.
- The proportion of respondents operating at normal capacity is elevated at 76%.
- In December, 20% of firms indicated that the single factor that is most limiting their ability to increase production is capacity. This is a marked lift from previous quarters.
- Together, this corresponds with the uplift in equipment investment we have seen through 2015-17.

Capacity utilisation



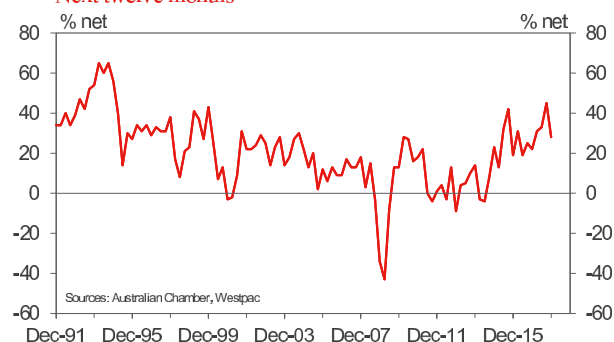
Profit expectations

	Q3 2017	Q4 2017
Net balance	45	28

- Manufacturing firms are expecting that profitability will continue to grow, with a positive outlook for 2018.
- A net 28% of respondents anticipate that profitability will rise over the next twelve months. This is a moderation of September's jump to a net 45% from a net 33% in March. However, December's assessment is still above the long-run average of 21%.
- The outlook is consistent with official measures of current profits. In the year to September, the ABS business indicators survey indicates that manufacturing profits have increased by 4.5%.

Profit expectations

Next twelve months



The labour market

Numbers employed *(seasonally adjusted)*

	Q3 2017	Q4 2017
Actual – net balance	13	13
Expected – net balance	11	15

- Firms are continuing to increase hiring in response to the lift in demand. Respondents have indicated that manufacturing employment has grown steadily through 2017 following a long period of contraction from 2011 to mid 2016.
- In December, a net 13% of firms indicated that they expanded their workforce. This is the same as September's net 13%, and just above June's net 12%.
- Official ABS data indicates that manufacturing employment has been stable in the year to August, a better result than previous year's of contraction. The stable outcome is despite the exiting of some automotive firms, with this dynamic now reaching its conclusion.

Overtime worked *(seasonally adjusted)*

	Q3 2017	Q4 2017
Actual – net balance	47	37
Expected – net balance	32	23

- Over the past five years, firms have indicated that they have increased the use of overtime in response to rising new orders and output.
- The momentum in overtime worked fell in December. This was foreshadowed by past survey results which showed a drop in the expected use. In December, a net 37% of firms report that they increased overtime, down from a net 47% in September.
- Persistent and widespread use of overtime is not the norm, and December's pullback is likely to be in relation with the increased hiring in the manufacturing sector. That said, a still net 37% increasing overtime is an above average proportion.

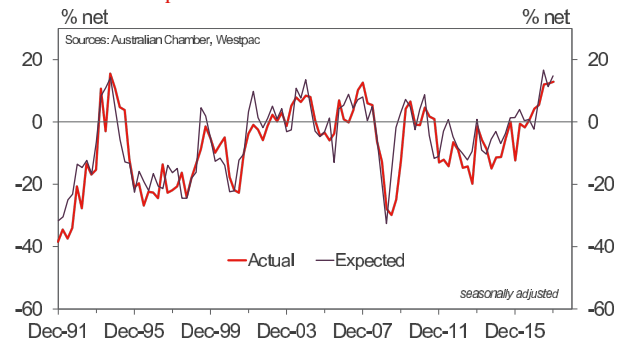
Difficulty of finding labour *(seasonally adjusted)*

	Q3 2017	Q4 2017
Net balance	3	1

- The survey provides insights into the tone of the overall labour market. Respondents' views on the difficulty of finding labour broadly tracks shifts in the unemployment rate for the Australian economy.
- A net 1% of respondents indicated that labour was harder to find in December, a little lower than a net 3% in September, and generally consistent with the results since mid 2016.
- The official ABS data suggests that the labour market has tightened through the year. The unemployment rate has gradually fallen from 5.9% in March to 5.4% in October with annual employment growth tracking at 3.0%.

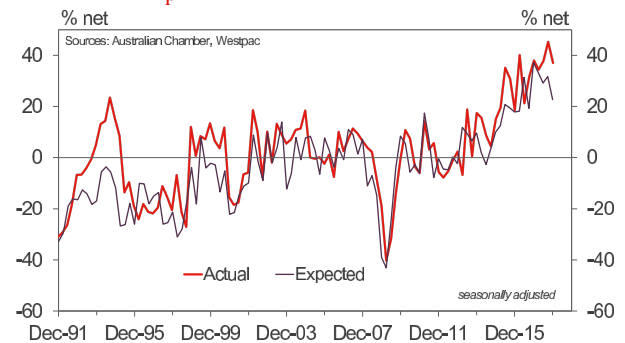
Numbers employed

Actual & expected

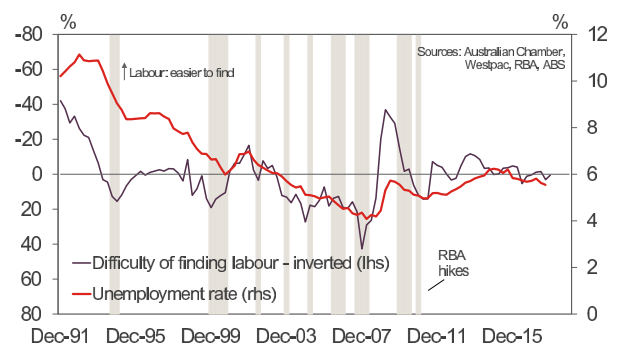


Overtime worked

Actual & expected



Labour market tightness



Prices & inflation

Average unit costs

	Q3 2017	Q4 2017
Actual – net balance	24	16
Expected – net balance	13	5

- In 2016, and in particular the first half of 2017, input price escalation has been a concern for firms. This comes after a period of subdued cost rises.
- In March a net 46% of respondents reported that unit costs had increased, and this was sustained further in June with a net 41%. The relatively high readings reflect a large jump in commodity and energy costs.
- With the initial price shock coming to pass, September showed a net 24% of firms indicating input price increases, which moderated further in December with a net 16% indicating increases.
- Electricity prices are still elevated and the issue remains fluid with a high degree of uncertainty.

Average selling prices

	Q3 2017	Q4 2017
Actual – net balance	4	4
Expected – net balance	9	11

- Price increases have been more prevalent since mid 2013, in contrast to the lack of pricing power which was the norm prior to 2008.
- In December, a net 4% of respondents indicated that they raised prices, in line with September's result but below June's net 16%.
- However, expectations have held up with a net 11% of firms reporting that they intend on increasing selling prices in the next three months.
- The lift in selling prices may be due to firms expecting to pass through earlier cost pressures or it could be in response to the persistent increase in demand.

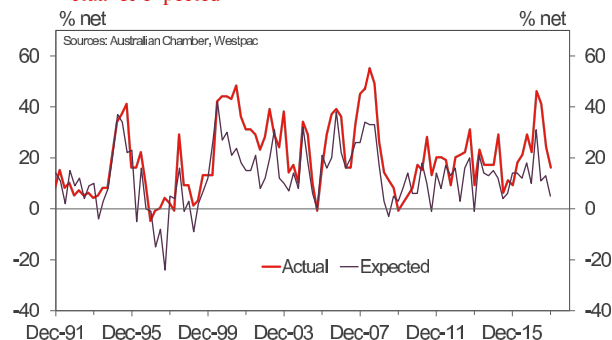
Manufacturing wages

	Q3 2017	Q4 2017
Net balance	11	6

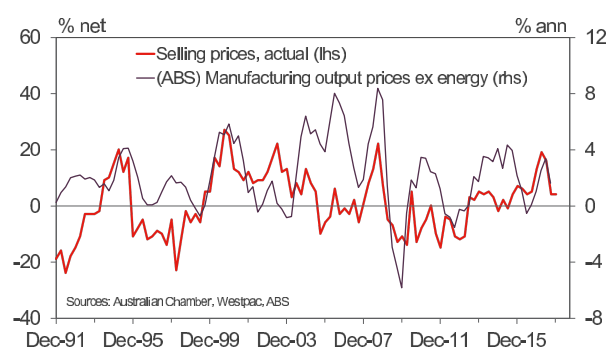
- The survey suggests a continuing lift in wages growth in the year ahead. A net 6% of firms expect that their next wage bill will deliver an outcome above the last.
- This is a second consecutive moderation from a net 11% in September and a net 16% in June. However, it is still above indications from a year ago.
- The survey results have deviated from official measures reported by the ABS over the past few years.
- However, recent indications have shown annual manufacturing wage growth pick up from a low of 1.8% at the end of 2016 to 2.2% as at Q3 2017, suggestive of a turning point.

Average unit costs

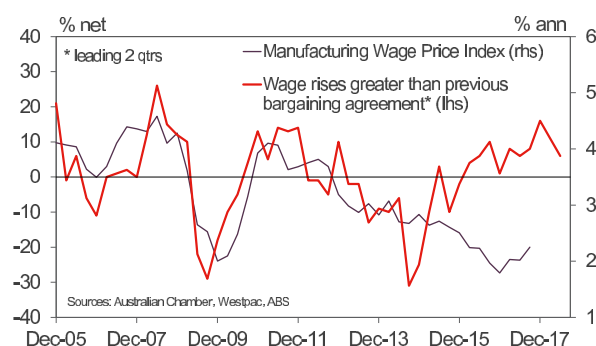
Actual & expected



Manufacturing upstream price pressures

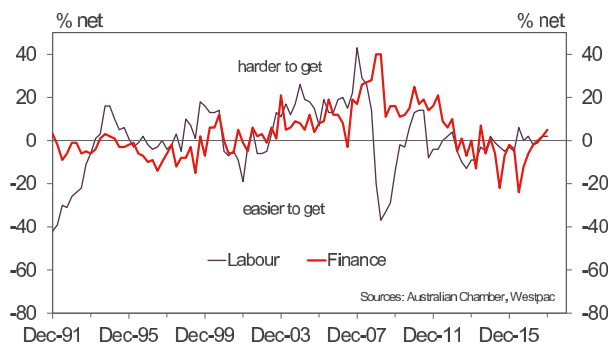


Manufacturing wage growth

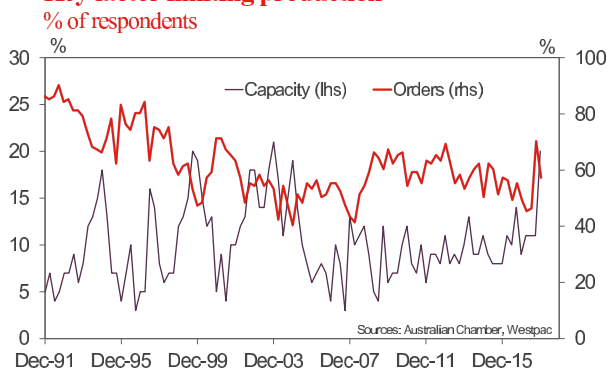


Other results

Availability of labour & finance

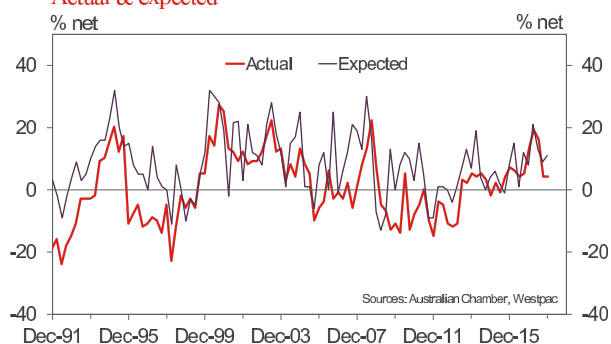


Key factor limiting production

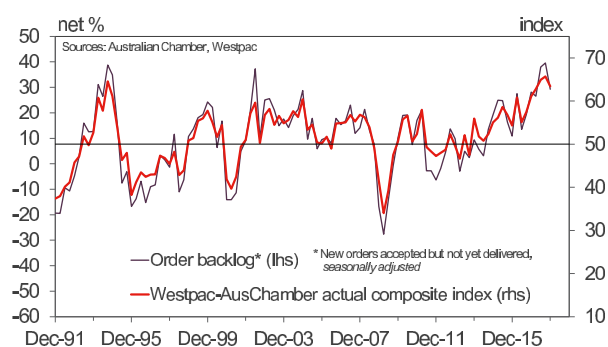


Average selling prices

Actual & expected

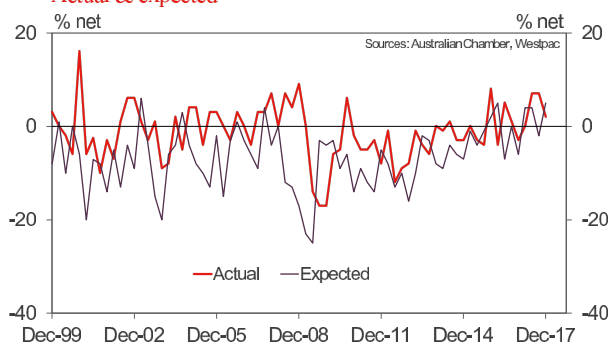


Order backlog & actual conditions



Stocks of finished goods

Actual & expected



Factors limiting production

	Q2 2017	Q3 2017	Q4 2017
Orders (%)	46	70	57
Capacity (%)	11	11	20
Labour (%)	3	2	3
Finance (%)	5	4	2
Materials (%)	0	0	2
Other (%)	26	12	12
None (%)	9	1	4

Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

Summary of results (not seasonally adjusted)

1. Do you consider that the general business situation in Australia will improve, remain the same, or deteriorate in the next six months?

Net balance	Improve	Same	Deteriorate
29	38	53	9

2. At what level of capacity utilisation are you working?

Net balance	Above Normal	Normal	Below Normal
0	12	76	12

3. What single factor is most limiting your ability to increase production?

None	4	Orders	57
Material	2	Finance	2
Labour	3	Capacity	20
Other	12		

4. Do you find it is now harder, easier, or the same as it was three months ago to get:

	Net balance	Harder	Same	Easier
(a) labour?	2	5	92	3
(b) finance?	5	9	87	4

5. Do you expect your company's capital expenditure during the next twelve month to be greater, the same, or less than the past year:

	Net balance	Greater	Same	Less
(a) on buildings?	2	10	82	8
(b) on plant & machinery?	15	23	69	8

Excluding normal seasonal changes, what has been your company's experience over the past three months & what changes do you expect during the next three months in respect of:

Change in position in the last 3 months					Expected change during the next 3 months			
	Net balance	Improve	Same	Down	Net balance	Improve	Same	Down
6. Numbers employed	12	17	78	5	10	12	86	2
7. Overtime worked	48	54	40	6	11	21	71	9
8. All new orders received	41	52	37	11	19	26	67	7
9. Orders accepted but not yet delivered	36	41	54	5	2	16	70	14
10. Output	42	48	46	6	14	21	72	7
11. Average costs per unit of output	16	20	76	4	5	11	83	6
12. Average selling prices	4	9	86	5	11	13	85	2
13. Export deliveries	4	6	92	2	3	8	87	5
14. Stock of raw materials	4	10	84	6	13	16	81	3
15. Stocks of finished goods	2	11	80	9	5	11	83	6

Summary of results (not seasonally adjusted)

16. Over the next twelve months do you expect your firm's profitability to:

(a) Improve?	35
(b) Remain unchanged?	58
(c) Decline?	7
Net balance	28

17. Do you expect your firm's next wage enterprise deal will produce annual rises which vis-a-vis the previous deal are:

(a) Greater?	14
(b) Same?	78
(c) Less?	8
Net balance	6

A. Industry profile of survey:

	(% of respondents)
Food, beverages, tobacco	13
Textiles, fabrics, floor coverings, felt, canvas, rope	4
Clothing, footwear	6
Wood, wood products, furniture	3
Paper, paper products, printing	10
Chemicals, paints, pharmaceuticals, soaps, cosmetics petroleum & coal products	12
Non-metallic mineral products: glass, pottery, cement bricks	5
Basic metal products: processing, smelting, refining, pipes & tubes	4
Fabricated metal products: structural & sheet metal, coating & finishing, wire, springs, hand tools	16
Transport equipment: motor vehicles & parts, excluding repairs, rail, ships, aircraft, including repairs	5
Other machinery & equipment: electrical, industrial scientific, photographic	11
Miscellaneous: including manufacturers of leather, plastic & rubber, sporting equipment, jewellery	12

B. How many employees are covered by this return?

1-100	101-200	201-1000	Over 1000
52	7	16	25

C. In which state is the main production to which this return relates?

WA	SA	VIC	NSW/ACT	QLD	TAS
12	10	18	44	13	4

The Westpac-AusChamber Composite Indices

The Westpac-AusChamber Actual and Expected Composite indices are weighted averages of the activity measures in the survey. The weights are as follows: employment 20%; new orders 30%; output 25%; orders accepted but not delivered 15%; overtime 10%.

The Westpac-AusChamber Labour Market Composite is a function of actual employment, with a weight of almost 50%, as well as: expected employment; expected overtime; new orders; order backlog; and expected order backlog.

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