

Australian Chamber–Westpac Survey of Industrial Trends

Australian Chamber of Commerce and Industry & Westpac Banking Corporation

222nd report March 2017 (survey conducted 1 February to 6 March 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 strengthened in March 2017, lifting 2.5pts to 63.0, extending the rebound from a dip to 55.0 in June 2016, coinciding with the July Federal election.
- The above par reading for the Composite index, which has trended higher since 2014, reflects strength across new orders, output, overtime, and employment. New orders were particularly strong in the March quarter, possibly including an element of catch-up after the soft spot in 2016.
- Manufacturing is benefitting from: a strong upswing in new home building activity, although rates of growth have moderated; a lift in renovation activity; an increase in competitiveness associated with the sharply lower currency, down 28% against the US dollar from the highs of early 2013; and a strengthening of conditions in manufacturing globally. Even so, there are some negatives. Mining investment is trending lower and consumer spending, while it rebounded in late 2016, has been lacklustre.
- The modest uptrend in exports appears to have resumed after stumbling in 2016, with a net 8% of respondents reporting a rise in export deliveries. Expectations are modestly positive, supported by the relatively low AUD, but constrained by weak world trade.
- Expectations are positive, centred on new orders and output as well as employment. The Expected Composite index is at 63.8 in March, up 1.6pts from December. A net 37% expect the general business environment to strengthen over the next six months, an upbeat mood, up from 25% in December.
- Businesses are looking to 2017 to be a positive year for profits, driven by rising turnover and a lower Australian dollar boosting export returns. A net 31% expect profits to rise in the 12 months ahead.
- Equipment investment intentions have been positive over the past two years, consistent with some reduction in the sector's spare capacity and improving profitability. A net 13% of firms expect to increase equipment spending in the next year. Investment plans for building investment are muted at a net +3%.
- The survey's Labour Market Composite, which broadly tracks economy wide jobs growth, was 54.5 in March, up from 51.7. A reading at this level points to robust jobs momentum in 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 222nd consecutive survey was closed on 6 March 2017.

A total of 285 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 May/June 2017.

Key survey results

Westpac–AusChamber Composites *(seasonally adjusted)*

	Q4 2016	Q1 2017
Actual – composite index	60.5	63.0
Expected – composite index	62.2	63.8

- The Westpac-AusChamber Actual Composite Index continued to rise, up to 63.0 in March 2017 from 60.5 in December. Momentum has steadily picked up after a dip to 55.0 in June.
- Contributors to the strong result are strength in new orders, rising output and overtime, as well as gains in employment.
- The elevated level in the Composite is in part a catch-up from softer activity in Q2 2016 related to uncertainty around the Federal election. Firms are benefitting from accommodative monetary policy and a lower currency, along with a cyclical rise in manufacturing evident globally.
- The Expected Composite Index is at 63.8 with expansion in new orders, output, overtime and employment.

Westpac–AusChamber Labour Market Composite

	Q4 2016	Q1 2017
Net balance	51.7	54.5

- The survey provides insights into economy wide employment growth. This highlights the key linkages between manufacturing and the household sector.
- The Westpac-AusChamber Labour Market Composite rose to 54.5 in March from 51.7 in December. A reading at this level points to robust economy wide job gains in 2017, potentially in the order of 2% annual growth.
- Such an outcome would represent a turnaround from 2016, when jobs growth in Australia surprised to the low side, slowing to annual growth of less than 1%.
- The Labour Market Composite is a function of actual employment, with a weight of around 50%, as well as expected employment, expected overtime, new orders, order backlog and expected order backlog.

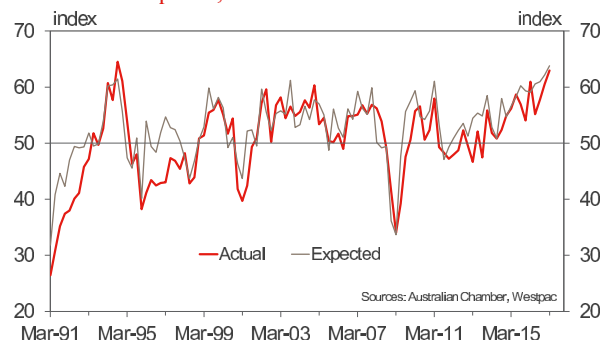
General business situation

	Q4 2016	Q1 2017
Net balance	25	37

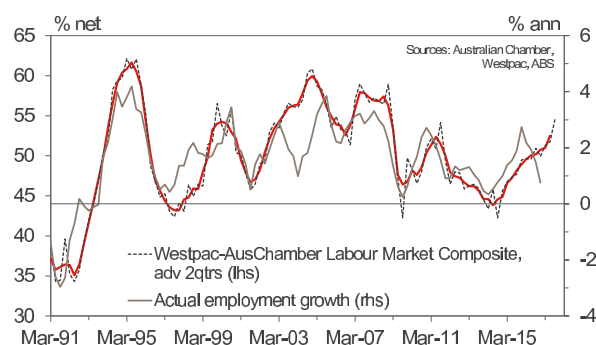
- The manufacturing sector is thinking positively in 2017. In March, a net 37% of respondents expect the business environment to improve over the next six months, up from 25% in December. Consistent with this, the Expected Composite index is elevated at 63.8.
- RBA rate cuts in May and August 2016 provided a timely boost to the economy. The home building upswing and a rebound in consumer spending late in 2016 are providing support to the manufacturing sector. A relatively low AUD is improving international competitiveness and boosting exports. In addition, state governments are investing more in new transport projects.

Westpac-AusChamber Composite indexes

Actual & expected, sa

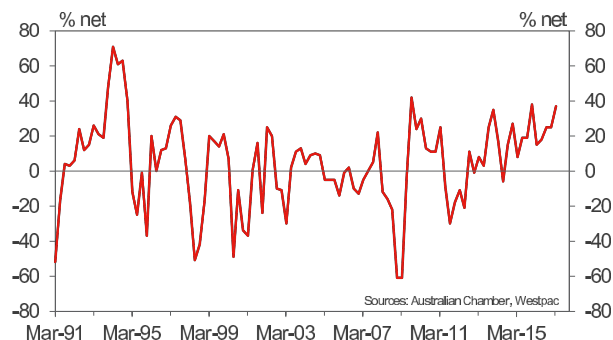


Employment: momentum picking up into 2017



General business situation

Next six months



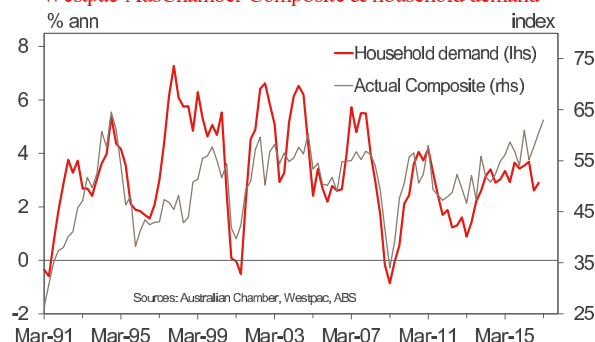
The business cycle & economic outlook

Manufacturing & the business cycle

- The Westpac-AusChamber Actual Composite has a solid track record of predicting near-term domestic economic conditions, including identifying turning points in the cycle.
- The Composite tracks movements in household demand, highlighting the key linkages between the consumer, home building (both new and renovations) and manufacturing.
- GDP grew by 1.1% in Q4 2016, a rebound from a soft Q3. Household demand was up 0.9% on the back of only 0.3% growth in Q3. This brought annual growth in household demand to 2.9%yr.
- The Actual Composite index strengthening further in the March quarter 2017 adds to the evidence that the Australian economy is emerging from the 2016 slowdown.

Manufacturing & the business cycle

Westpac-AusChamber Composite & household demand

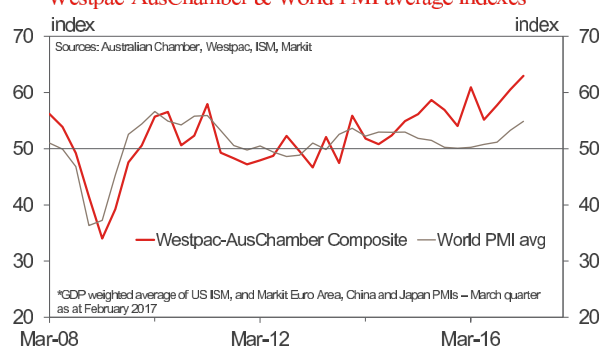


Australian & World manufacturing surveys

- Global and Australian manufacturing cycles have historically been highly synchronised, particularly at major turning points.
- The Westpac-AusChamber Actual Composite has tended to closely follow global manufacturing indexes. In 2014, the manufacturing sector outperformed as easier monetary conditions triggered a sharp upswing in home building activity.
- More recently, manufacturing conditions across the globe have strengthened, as is evident in the US, Europe and China. Very accommodative monetary policy internationally is contributing to the lift in business conditions globally.

Australian & World manufacturing surveys

Westpac-AusChamber & World PMI average indexes

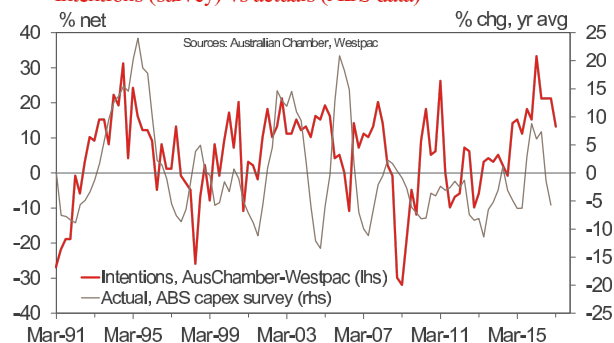


Manufacturing & business investment

- The AusChamber-Westpac survey has a solid track record of predicting equipment investment by the manufacturing sector.
- Businesses are looking to invest with a net 13% of respondents intending to increase plant & equipment investment in March. However, this marks a pull back from a net 21% in December, after the survey had trended up sharply from late 2014.
- The official ABS capex survey reports that actual manufacturing equipment investment grew by 7.3% in the 2015/16 financial year. The 2016/17 year has begun on a softer note, with year average growth slipping to -5.7% in December. The AusChamber-Westpac survey suggests that this will be a short lived dip.

Manufacturing equipment investment

Intentions (survey) vs actuals (ABS data)



Activity & orders

Output *(seasonally adjusted)*

	Q4 2016	Q1 2017
Actual – net balance	27	26
Expected – net balance	37	34

- Manufacturing output advanced solidly for an eleventh consecutive quarter, a trend that emerged during the second half of 2014 and has extended into 2017. In March, a net 26% of firms expanded output.
- While the trend is positive of late, volatility is evident. Output dipped late in 2015, to +15, as interest rates increased, and dipped again in mid-2016, to +14, dented by uncertainty ahead of the July Federal election.
- Expectations are positive, with a net 34% expecting to lift output in the next three months. Two RBA rate cuts in 2016, a rebound in conditions from the mid 2016 lull and a strengthening of global conditions have provided a positive start to 2017.

New orders *(seasonally adjusted)*

	Q4 2016	Q1 2017
Actual – net balance	26	36
Expected – net balance	33	42

- New orders gained materially for the 11th consecutive quarter, underpinning the lift in output.
- A net 36% of firms reported an increase in new orders in March. This is a step-up from a net 26% in December.
- Expectations point to further strength. A net 42% of respondents in March see an increase in new orders over the next three months, up from a net 33% in December.
- It may be that, in part, the strength of new orders early in 2017 includes an element of catch-up after the soft spot in 2016. In short, some businesses delayed spending decisions around the time of the July Federal election.

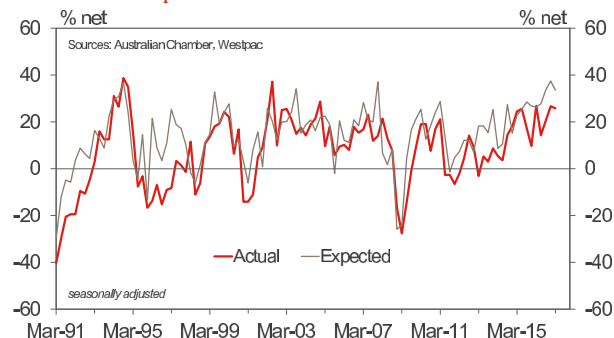
Exports

	Q4 2016	Q1 2017
Actual – net balance	6	8
Expected – net balance	5	8

- The uptrend in exports resumed in March with a net 8% of firms indicating higher export deliveries.
- Exports had advanced consistently from the second half of 2013 to early 2016 but stumbled in June 2016 when a net 3% of respondents reported lower exports.
- The relatively low level of the AUD has increased international competitiveness, supporting manufacturing firms despite sluggish world trade.
- A net 8% of respondents in March are expecting higher export volumes over the next three months.

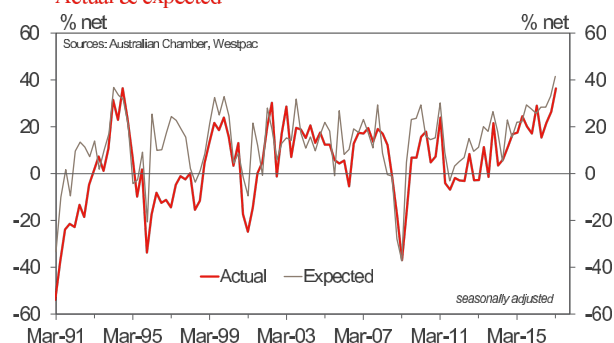
Output growth

Actual & expected



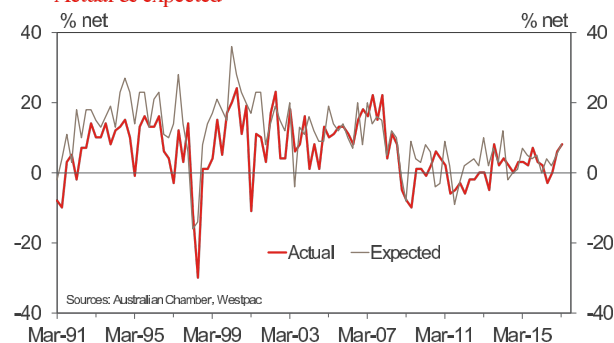
New orders

Actual & expected



Export deliveries

Actual & expected



Investment & profitability

Investment intentions

	Q4 2016	Q1 2017
Plant & Equipment – net balance	21	13
Building – net balance	6	3

- The survey, as it has since late 2014, points to an upswing in equipment investment in the manufacturing sector.
- In March, a net 13% of respondents expected to increase spending on plant and equipment in the next twelve months. While this is a moderation from a net 21% in December, it is still a very positive outcome. Building investment intentions are less upbeat, with only a net 3% expecting to increase spending.
- The official ABS capex survey reports that actual manufacturing equipment investment grew by 7.3% in the 2015/16 financial year. The 2016/17 year has begun on a softer note, with year average growth slipping to -5.7%. The AusChamber-Westpac survey suggests that this will be a short-lived dip.

Capacity utilisation

	Q4 2016	Q1 2017
Net balance	-5	-2

- Capacity utilisation levels trended higher from late 2013 and have consolidated at a relatively high level over the past 18 months.
- In the March quarter, the number of respondents operating above normal capacity was less than those operating below by a net 2%. That is in line with the recent average but well up from the net -20% readings prior to mid-2014.
- Looking over recent years, this trend is evidence that the upturn in business conditions is absorbing some of the spare capacity in the sector.
- More recently, the increase in equipment investment has been adding capacity to meet rising demand.

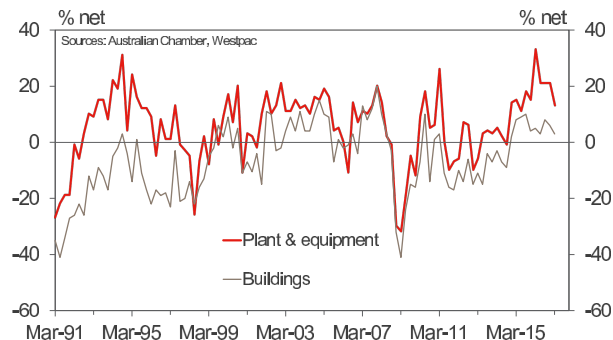
Profit expectations

	Q4 2016	Q1 2017
Net balance	22	31

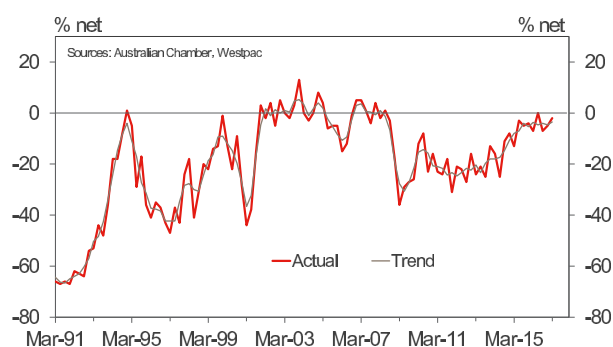
- Firms are looking to 2017 to be a positive year for profits.
- A net 31% of respondents expect profitability to increase in the next twelve months, up from a reading of 22% in December and exceeding the long-run average of the series, +19%.
- Expectations that profitability will improve are consistent with the positive outlook for output and new orders.
- Having said that, profit expectations are down from the highs reported during 2015. Notably, cost escalations have re-emerged as an issue for manufacturers.

Investment intentions

Next twelve months

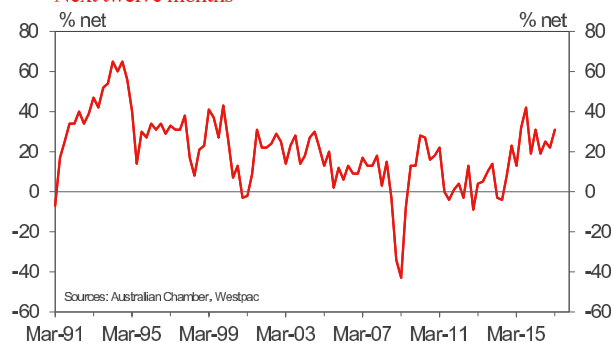


Capacity utilisation



Profit expectations

Next twelve months



The labour market

Numbers employed *(seasonally adjusted)*

	Q4 2016	Q1 2017
Actual – net balance	3	5
Expected – net balance	-4	7

- Manufacturers' views on hiring strengthened in 2016 and into 2017.
- In March, a net 5% of firms reported expanding their workforce, up from a net 3% in December. That follows a consolidation over the first half of 2016 and suggests a turnaround from the declines of recent years.
- The ongoing output expansion evident over the past two years has created the need for manufacturers to increase their workforce.
- However, the durability of the employment expansion remains uncertain. Expectations are positive for now, with a net 7% of respondents looking to expand their workforce in the coming three months.

Overtime worked *(seasonally adjusted)*

	Q4 2016	Q1 2017
Actual – net balance	36	35
Expected – net balance	37	34

- Over the past four years, respondents to the survey have indicated that they have increased overtime in response to rising new orders.
- The survey appears to suggest that the use of overtime has been more widespread of late than in the past. Persistent strength in overtime is atypical.
- In March, overtime again played a key role. A net 35% of respondents increased overtime in the period, in line with a net 36% in December. A net 34% expect to increase overtime in the coming three months.

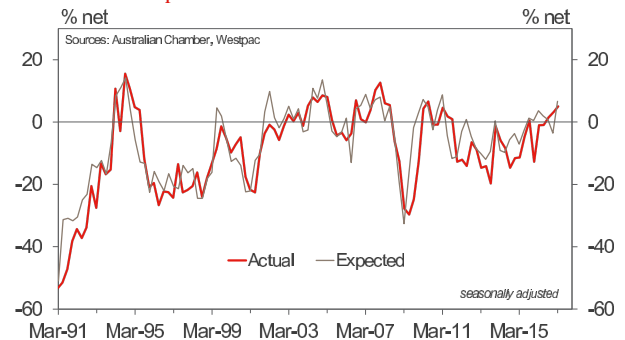
Difficulty of finding labour *(seasonally adjusted)*

	Q4 2016	Q1 2017
Net balance	0	-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 as a whole.
- In the March quarter, a net 1% of respondents reported labour as easier to find, not greatly different to recent updates.
- The official ABS data has been mixed. The unemployment rate has been relatively stable since March 2016. However, the underlying slack in the labour market has increased with sluggish jobs growth not keeping pace with the rising population.

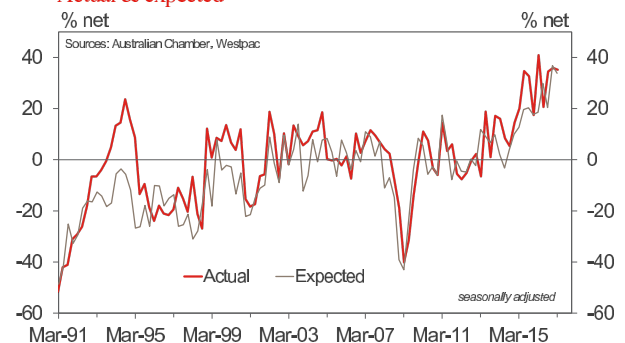
Numbers employed

Actual & expected

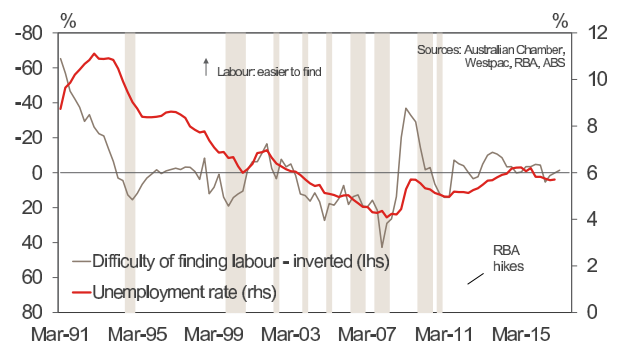


Overtime worked

Actual & expected



Labour market tightness



Prices & inflation

Average unit costs

	Q4 2016	Q1 2017
Actual – net balance	22	46
Expected – net balance	10	31

- In 2016 and into 2017, cost escalation re-emerged as an issue for manufacturers. This follows a period in which cost rises were subdued.
- A net 46% of firms reported a rise in unit costs in March, up from 22% in December and well up from 14% in 2015.
- The increase in cost pressures is against a backdrop of a bounce in commodity prices, up from historic lows, as well as higher electricity prices.
- Prior to this, average cost pressures had been relatively modest despite the sharp fall in the currency, evidence of the lack of domestic inflation pressures, with weak wages growth a key dynamic.

Average selling prices

	Q4 2016	Q1 2017
Actual – net balance	13	19
Expected – net balance	8	21

- Price rises for manufacturers have been more prevalent since mid-2013, in contrast to the lack of pricing power which was the norm post GFC.
- In March, a net 19% of firms reported an increase in prices, up from 13% in December. For the upcoming three months, a net 21% expect selling prices to rise.
- Most likely these results are evidence that earlier rises in import costs and, more recently, rising commodity prices are flowing through the pricing chain, often with a lag. Manufacturers are unlikely to have the scope to fully absorb the impact of the 28% fall in the currency since early 2013 and the recent jump in some commodity prices.

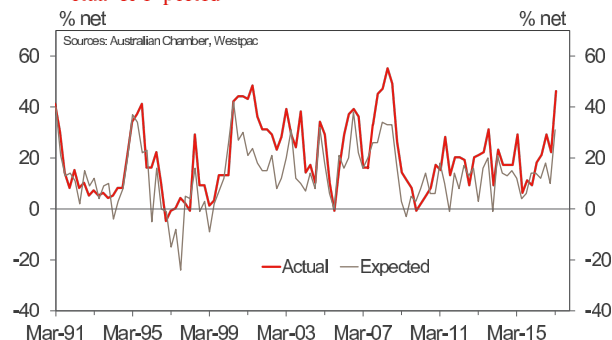
Manufacturing wages

	Q4 2016	Q1 2017
Net balance	6	8

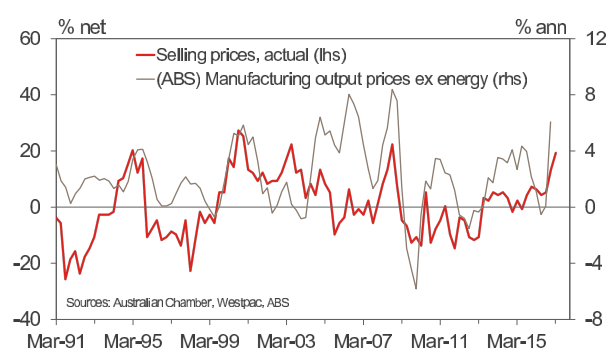
- The survey provides a guide to wage growth prospects for the manufacturing sector, correctly foreshadowing the marked slowing of wages growth evident since 2012.
- The survey points to a strengthening in wages growth in the year ahead. In March, a net 8% of firms expected their next wage deal to deliver an outcome above the last.
- To date, the official data continues to report weak wages growth. This has been a key feature of the broader Australian labour market, as well as the manufacturing sector. Significantly, national income has been squeezed by earlier sharp falls in the terms of trade. In 2016, the terms of trade have rebounded.

Average unit costs

Actual & expected



Manufacturing upstream price pressures

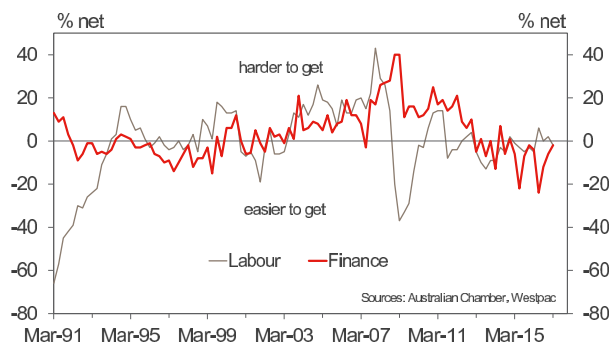


Manufacturing wage growth



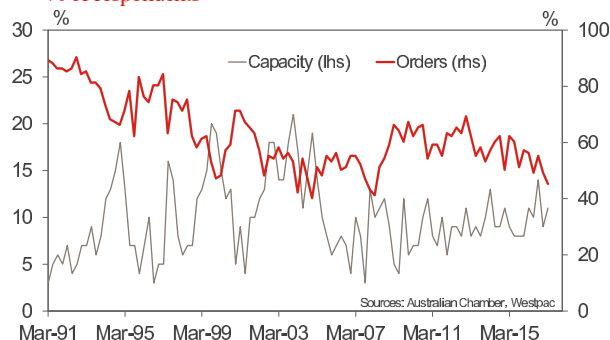
Other results

Availability of labour & finance



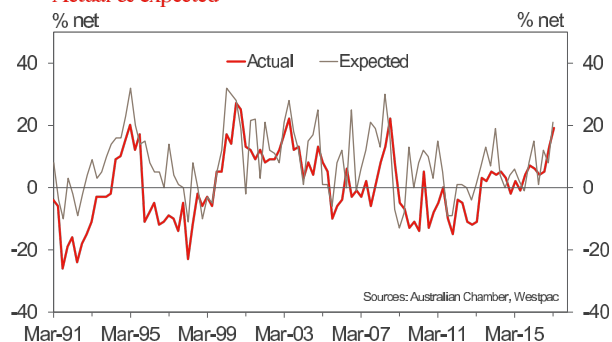
Key factor limiting production

% of respondents

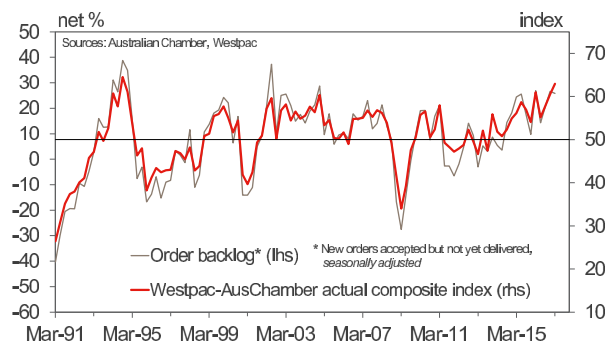


Average selling prices

Actual & expected

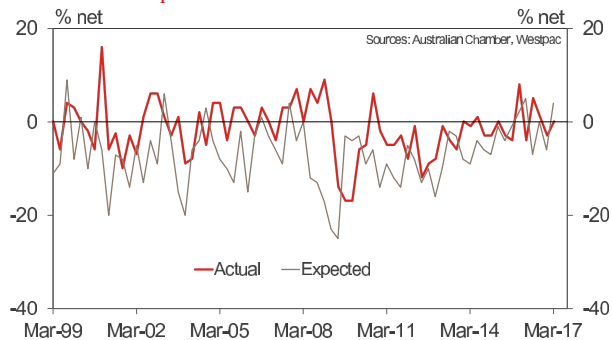


Order backlog & actual conditions



Stocks of finished goods

Actual & expected



Factors limiting production

	Q3 2016	Q4 2016	Q1 2017
Orders (%)	55	49	45
Capacity (%)	14	9	11
Labour (%)	2	2	2
Finance (%)	4	2	5
Materials (%)	3	1	1
Other (%)	13	25	22
None (%)	9	12	14

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
37	46	45	9

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

Net balance	Above Normal	Normal	Below Normal
-2	20	58	22

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

None	14	Orders	45
Material	1	Finance	5
Labour	2	Capacity	11
Other	22		

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	3	92	5
(b) finance?	-2	4	90	6

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?	3	14	75	11
(b) on plant & machinery?	13	24	65	11

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	4	11	82	7	10	12	86	2
7. Overtime worked	29	38	53	9	39	42	55	3
8. All new orders received	33	47	39	14	51	56	39	5
9. Orders accepted but not yet delivered	24	29	66	5	18	22	74	4
10. Output	19	33	53	14	41	45	51	4
11. Average costs per unit of output	46	48	50	2	31	32	67	1
12. Average selling prices	19	21	77	2	21	22	77	1
13. Export deliveries	8	12	84	4	8	11	86	3
14. Stock of raw materials	2	11	80	9	5	11	83	6
15. Stocks of finished goods	0	12	76	12	4	11	82	7

Summary of results (not seasonally adjusted)

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

(a) Improve?	41
(b) Remain unchanged?	49
(c) Decline?	10
Net balance	31

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?	15
(b) Same?	78
(c) Less?	7
Net balance	8

A. Industry profile of survey:

	(% of respondents)
Food, beverages, tobacco	16
Textiles, fabrics, floor coverings, felt, canvas, rope	3
Clothing, footwear	6
Wood, wood products, furniture	2
Paper, paper products, printing	8
Chemicals, paints, pharmaceuticals, soaps, cosmetics petroleum & coal products	12
Non-metallic mineral products: glass, pottery, cement bricks	4
Basic metal products: processing, smelting, refining, pipes & tubes	1
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	16
Miscellaneous: including manufacturers of leather, plastic & rubber, sporting equipment, jewellery	11

B. How many employees are covered by this return?

1-100	101-200	201-1000	Over 1000
49	10	23	18

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

WA	SA	VIC	NSW/ACT	QLD	TAS
12	11	24	34	14	5

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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Things you should know.

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