

Australian Chamber–Westpac Survey of Industrial Trends

Australian Chamber of Commerce and Industry & Westpac Banking Corporation

227th report June 2018 (survey conducted 9 May to 4 June 2018)

- 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 lifted in June 2018, up to 63.8 from 59.4 in March. The rise in June broke two quarters of moderation from 65.7 in September which was preceded by a sustained uptrend that emerged in June 2016 when the index was at 54.8.
- The above par reading for the Composite index reflects strength in new orders, output, overtime and backlog. However, employment consolidated in June after the hiring burst in the second half of 2017.
- Manufacturing is benefitting from: a strong upswing in public infrastructure investment with state governments continuing to add new projects to the pipeline, as well as solid non–residential business construction and a relatively low Australian dollar combined with an above par pace of global growth. Against this are negatives relating to moderate consumer spending constrained by low wage growth and continuing intensity from offshore competition. The homebuilding upswing is also fading from high levels as the housing market cools.
- The uptrend in exports has continued at a moderate pace after stumbling back in 2016. The speed of expansion slowed in June as global growth began the year on a softer note following 2017’s uplift. A net 3% of firms report an increase in export deliveries in June. Export expectations in June are similarly positive but are also down slightly from March.
- Expectations are positive, centred on new orders, output, backlog, overtime as well as renewed expansion in employment. The Expected Composite rose to 66.8 in June from 61.0 in March which takes the index back above the mid–2017 peak of 64.9. A net 37% expect the general business situation to improve over the next six months, continuing the upbeat mood.
- Equipment investment intentions of respondents have been positive over recent years in response to rising demand. This is consistent with rising profitability and high levels of capacity utilisation. A net 22% of firms intend to increase equipment investment over the next year. Building intentions are solid, a net 7% of firms expect to increase investment, up from a net 3% in March.
- The survey’s Labour Market Composite, which broadly tracks economy–wide jobs, is at 55.1. The index correctly foreshadowed the acceleration in employment through 2017 and identified the turning point to softer momentum in early 2018. The current positive level of the index suggests employment growth will pick–up to a solid pace over the remainder of 2018 but remain short of 2017’s outsized expansion.

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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 227th consecutive survey was closed on 4 June 2018.

A total of **271** 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 August/September 2018.

Key survey results

Westpac-AusChamber Composites *(seasonally adjusted)*

	Q1 2018	Q2 2018
Actual - composite index	59.4	63.8
Expected - composite index	61.0	66.8

- The Westpac-AusChamber Actual Composite Index bounced to 63.8 in June from 59.4 in March. This follows softening in the past two quarters from September's top of 65.7.
- The Composite is back to a well above average level with output, new orders, overtime and backlog all seeing strength. However, employment softened after a hiring burst through the second half of 2017.
- Public infrastructure investment is boosting demand in the manufacturing sector which is also supported by solid non-mining business investment and a relatively low AUD.
- The Expected Composite rose to 66.8 from 61.0 suggesting the rebound has further to play out.

Westpac-AusChamber Labour Market Composite

	Q1 2018	Q2 2018
Net balance	52.9	55.1

- 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 increased to 55.1 from 52.9.
- The index correctly led the uplift in employment in 2017. Official data report that employment growth was a brisk 3.2% in 2017.
- Similarly, the plateau and turn lower in the index led 2018's employment slowdown. The current four month annualised pace to April is just 1.3%.
- The stabilisation in the Composite points to employment growth improving to a solid pace but well short of what we saw in 2017.

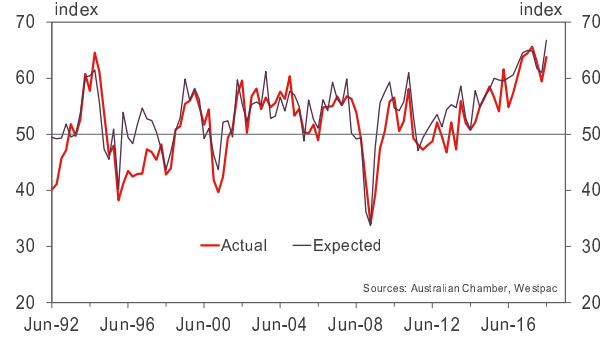
General business situation

	Q1 2018	Q2 2018
Net balance	38	37

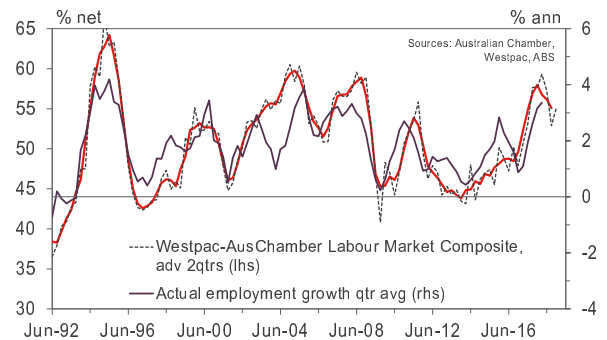
- Manufacturing firms are positive on the business environment. In June, a virtually unchanged net 37% of respondents expect the general business environment to improve over the next six months. The upbeat outlook is consistent with results in March and over 2017.
- The June survey took place post the May Federal Budget and manufacturers' continued optimism suggests this year's policy reinforced the mood.
- Growth in many advanced economies slowed in the first quarter of 2018 following the uplift in 2017. However, it would appear that continued state infrastructure investment at home has offset the diminishing external demand and kept domestic sentiment elevated.

Westpac-AusChamber Composite indexes

Actual & expected, sa

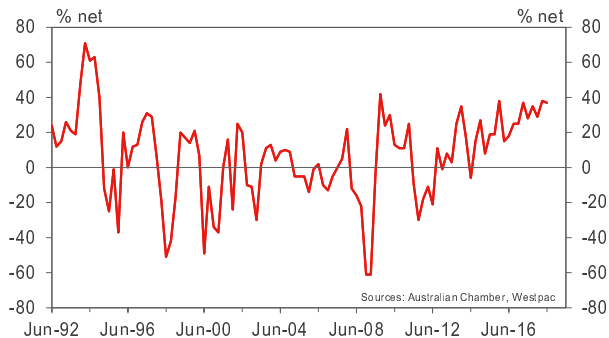


Employment: momentum may be peaking



General business situation

Next six months



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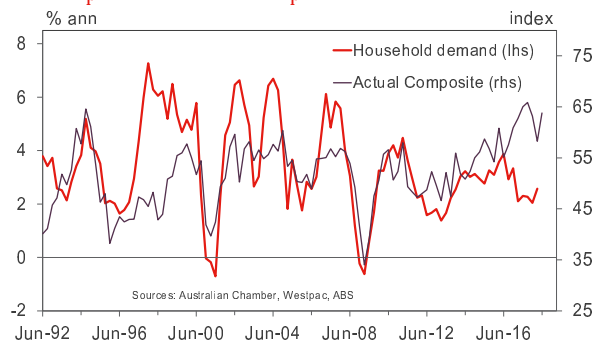
The business cycle & economic outlook

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.
- Recently manufacturing has been mainly supported by activity outside of the household sector.
- The major development boosting manufacturing is increased public infrastructure investment. Other contributing drivers are solid non-mining business investment as well as a relatively low AUD and above average world growth.
- Official data confirms that manufacturing is expanding. The national accounts showed manufacturing output increased by 2.4% in the March quarter. That followed 2017 marking the first year of annual manufacturing growth since 2011.

Manufacturing & the business cycle

Westpac-AusChamber Composite & household demand

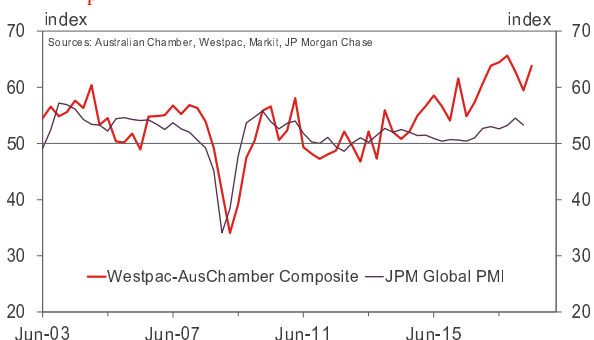


Australian & World manufacturing surveys

- 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 conditions.
- However, since 2014, the Composite has deviated to the upside. In part this reflects Australian outperformance as easier monetary policy led to an upswing in homebuilding, but it also reflects the transitional effect of exiting firms. More recently, a public infrastructure upswing is boosting activity.
- Global manufacturing expanded in 2017 in line with the uplift in world growth. Activity has slowed in 2018 and conditions have diverged across countries. Europe and Asia are falling back from the previous jump while the US is gaining momentum on the back of expansionary fiscal policy.

Australian & World manufacturing surveys

Westpac-AusChamber & Global PMI indexes

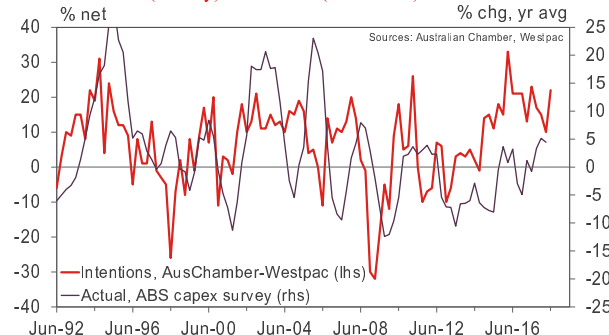


Manufacturing & business investment

- The AusChamber-Westpac survey has a solid track record of predicting equipment investment from the manufacturing sector.
- Manufacturing firms are expecting to invest over the next year. A net 22% of respondents are intending to increase plant and equipment investment in the next twelve months.
- The ABS capex survey confirms that manufacturing investment is expanding. The 2017/18 financial year is shaping up strongly with real manufacturing equipment investment up 4.5% in the year to the March quarter 2018. This follows a softer 2016/17 and a strong uplift in 2015/16.

Manufacturing equipment investment

Intentions (survey) vs actuals (ABS data)



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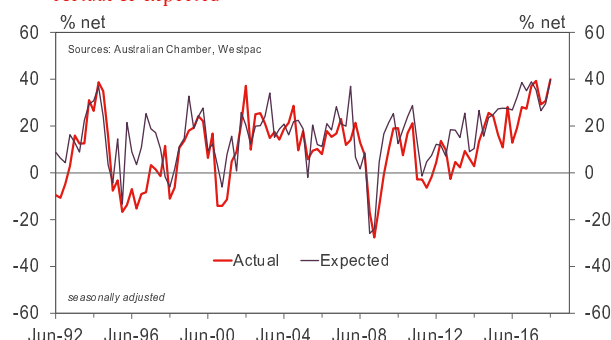
Activity & orders

Output *(seasonally adjusted)*

	Q1 2018	Q2 2018
Actual - net balance	31	40
Expected - net balance	30	40

- Manufacturing output has now expanded for sixteen consecutive quarters. A net 40% of respondents reported higher output in June.
- The uptrend emerged in 2014 and gradually picked up momentum. After a modest dip in the last few quarters, the June rebound has re-established the expansionary trend.
- Expectations mirrored the move in actual output. In June, a net 40% of firms expect output to increase in the next three months.

Output growth Actual & expected

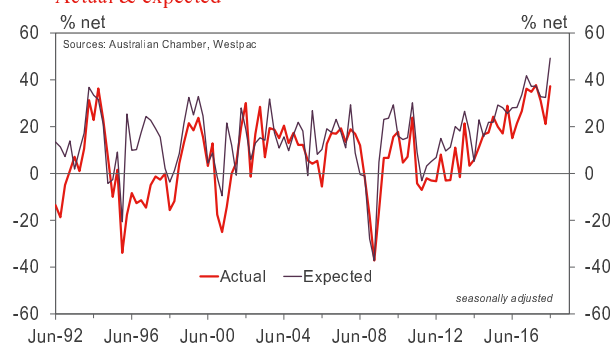


New orders *(seasonally adjusted)*

	Q1 2018	Q2 2018
Actual - net balance	21	37
Expected - net balance	32	49

- Increasing new orders are behind the expansion in manufacturing output. In June, a net 37% of firms indicated an increase in new orders.
- The expectations sub-index previously held up in the March survey which suggested that the dip in output in the quarter would be short-lived.
- In the June survey, a net 49% of respondents anticipate that new orders will increase in the next three months. This indicates that activity has resumed its uptrend and momentum should continue into the second half of the year.
- Public infrastructure investment is strong and with state governments continuing to add new projects to the pipeline, new orders are expanding.

New orders Actual & expected

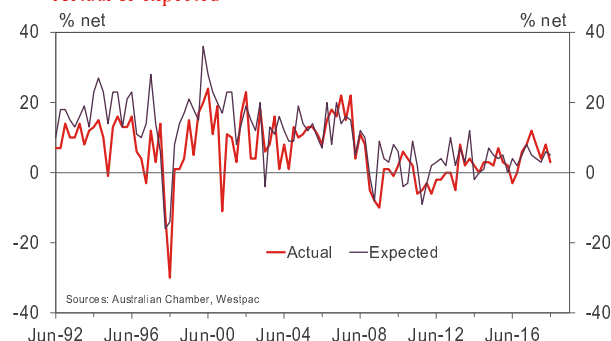


Exports

	Q1 2018	Q2 2018
Actual - net balance	8	3
Expected - net balance	6	5

- Exports increased at a slower pace in June than March and the average over 2017. A net 3% of firms reported that exports rose in June.
- That is consistent with some slowing in global growth in 2018 after 2017's synchronised uplift. Correspondingly, the Australian dollar has depreciated in the last few months providing some offset from the slowing in overall demand.
- Expectations show a net 5% of respondents seeing higher exports in the next three months.

Export deliveries Actual & expected



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Investment & profitability

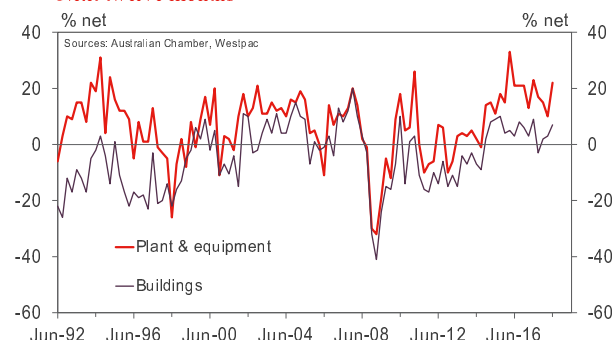
Investment intentions

	Q1 2018	Q2 2018
Plant & Equipment - net balance	10	22
Building - net balance	3	7

- The survey, as it has since late 2014, indicates that manufacturing firms are intending to increase investment in response to rising demand and consistent with upbeat business sentiment.
- In June, a net 22% of respondents report that they are planning to increase equipment investment over the next twelve months. This is well up on March's net 10% and is back to levels seen around 2015-16.
- Building investment intentions also tracked higher, a net 7% of respondents seeing increased building in the next twelve months compared to a net 3% in March.

Investment intentions

Next twelve months

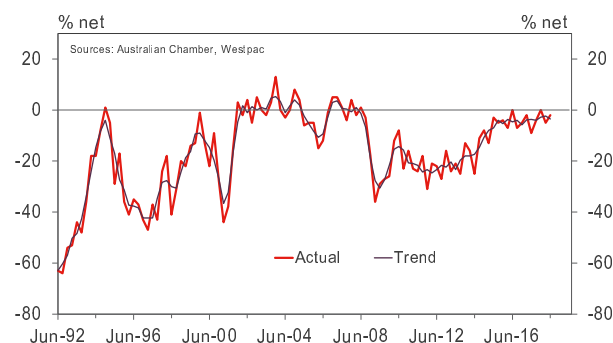


Capacity utilisation

	Q1 2018	Q2 2018
Net balance	-5	-2

- Capacity utilisation has maintained an elevated level following the uplift seen from late 2013 to late 2015.
- The number of firms operating above normal capacity was less than the number of firms below normal capacity by a net 2%. Three quarters are at normal capacity levels. This is broadly in line with the reports over the last few years.
- A net 16% of firms indicate that the single factor that is limiting their ability to increase production is capacity. That figure was the same in the March survey. Strong demand and capacity pressures are likely to continue to be a support for higher equipment investment.

Capacity utilisation



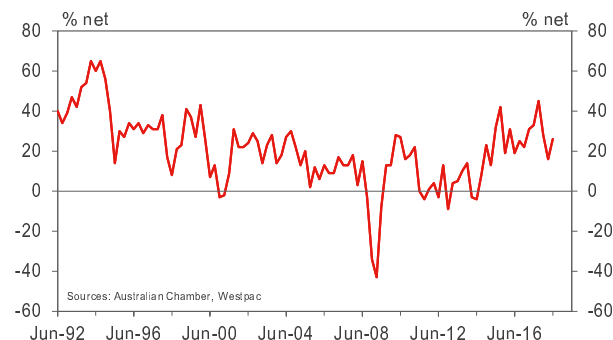
Profit expectations

	Q1 2018	Q2 2018
Net balance	16	26

- Manufacturing firms expectations on profitability rebounded in June, consistent with the bounce in output and new orders.
- A net 26% of respondents are anticipating that profitability will rise over the next twelve months. That is up from March's net 16% and back to being in line with December's net 28%.
- Official data confirms that profitability has improved. The ABS business indicators survey shows that manufacturing gross operating profits rose 9.6% in the year to March 2018.

Profit expectations

Next twelve months



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The labour market

Numbers employed *(seasonally adjusted)*

	Q1 2018	Q2 2018
Actual - net balance	1	-3
Expected - net balance	-6	7

- The survey indicates that manufacturing employment softened in the June quarter as indicated by the March survey's negative expectations reading. A net 3% of firms reported that they decreased their workforce in June.
- This is the first decline in actual employment since June 2016. Output cooled in the first quarter of 2018 and potentially led to more cautious hiring activity. The moderation also follows the burst in hiring seen in late 2017 and suggests that the uplift may have been a little over done.
- Expectations suggest that the reduction in the workforce will not last long. A net 7% of firms expect to expand hiring in the next three months ahead.

Overtime worked *(seasonally adjusted)*

	Q1 2018	Q2 2018
Actual - net balance	9	37
Expected - net balance	20	43

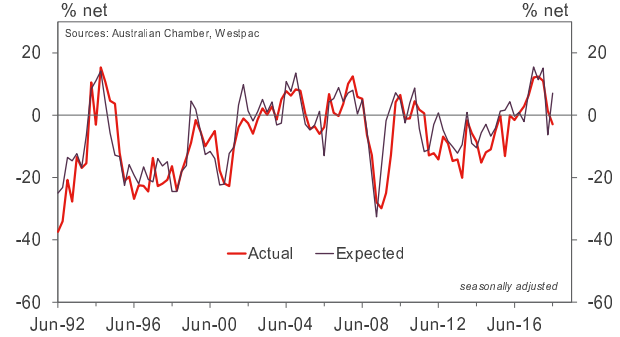
- Overtime worked jumped sharply in June after a steep decline in March. A net 37% of firms indicated that they increased overtime in June.
- That brings it back to the elevated levels seen over the past few years with an increased use of overtime present since late 2012.
- The lift in output in June was behind the need for longer overtime. A net 43% of respondents expect to increase overtime in the next three months despite the similarly driven expectations for a larger workforce.

Difficulty of finding labour *(seasonally adjusted)*

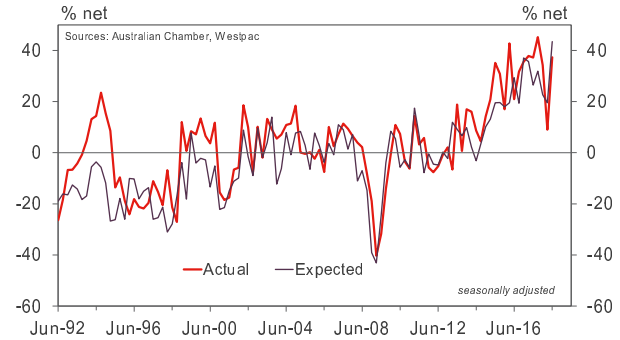
	Q1 2018	Q2 2018
Net balance	10	2

- The survey provides insights into the tone of the overall labour market. Firms' views on the difficulty of finding labour broadly tracks shifts in the unemployment rate for the Australian economy.
- A net 2% of firms report that labour was harder to find in June, down from a net 10% in March. This brings the survey measure back into line with results seen over the previous few years.
- Official ABS data indicates that progress on reducing the unemployment rate has stalled after some tightening seen earlier. In April 2018, the unemployment rate is 5.6% with moves in the participation rate having tended to mirror changes in employment over the past year.

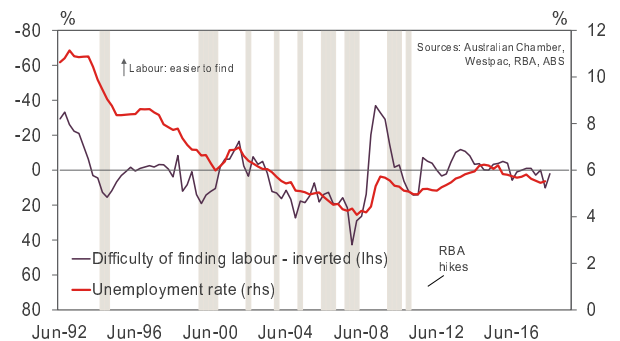
Numbers employed Actual & expected



Overtime worked Actual & expected



Labour market tightness



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Prices & inflation

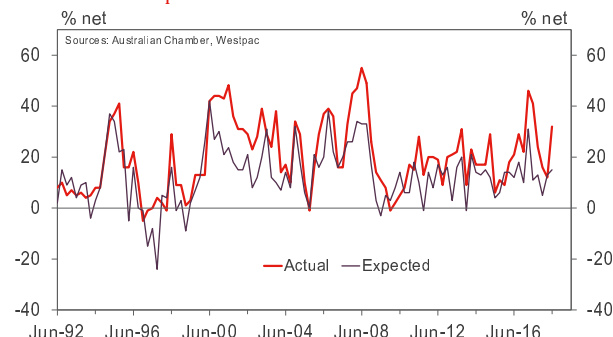
Average unit costs

	Q1 2018	Q2 2018
Actual - net balance	12	32
Expected - net balance	13	15

- In 2016, and in particular the first half of 2017, input cost escalation was a concern for firms. This follows a period of subdued cost rises.
- The issue has re-emerged in June with a net 32% of respondents indicating that unit costs have increased.
- While the previous period centred on a spike in electricity costs, on this occasion, increases relate to a rally in oil and base metal prices.
- That is not to mention that electricity costs remain elevated and resolving the issue is likely to take time.

Average unit costs

Actual & expected

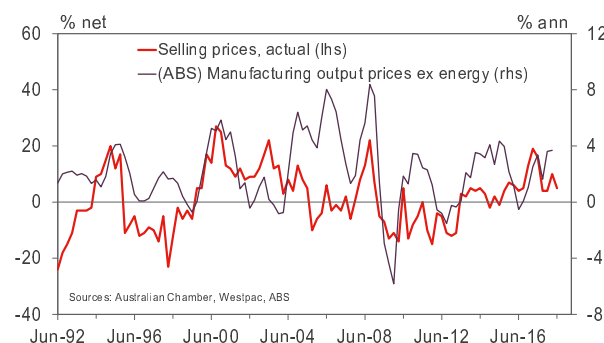


Average selling prices

	Q1 2018	Q2 2018
Actual - net balance	10	5
Expected - net balance	12	7

- Price increases have become more prominent since mid 2013, in contrast to the lack of pricing power which was the norm prior to 2008.
- However, despite the rise in input costs, a net 5% of firms increased prices in June down from a net 10% in March. Expectations are also lower with a net 7% of respondents anticipating to increase prices in the next three months compared to a net 12% in March.
- This suggests that in the current circumstance, firms are price takers. It may be that rising volumes have allowed firms to withstand some margin pressure.

Manufacturing upstream price pressures

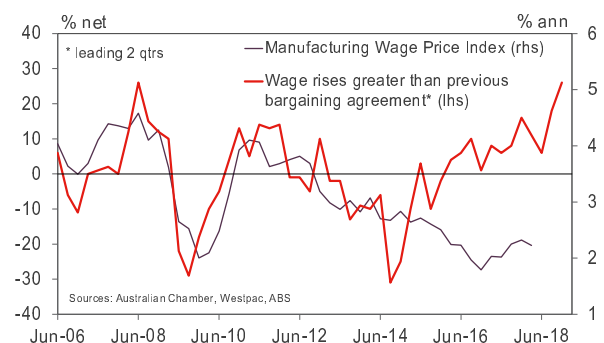


Manufacturing wages

	Q1 2018	Q2 2018
Net balance	18	26

- The survey indicates that manufacturing wages will increase in the year ahead. In June, a net 26% of firms expect that their next wage bill will deliver an outcome above the last.
- While survey measures have differed from the data reported by the ABS over the past few years, official measures of manufacturing wages have stabilised and begun to trend higher.
- The latest wage price index update indicated that momentum eased off but the AusChamber-Westpac survey result suggests that the nascent uptrend should reassert itself (although potentially at a gradual pace).

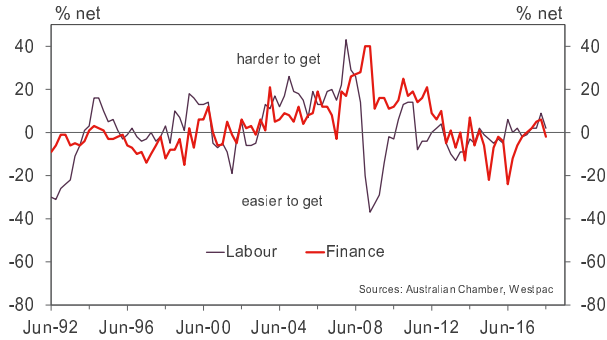
Manufacturing wage growth



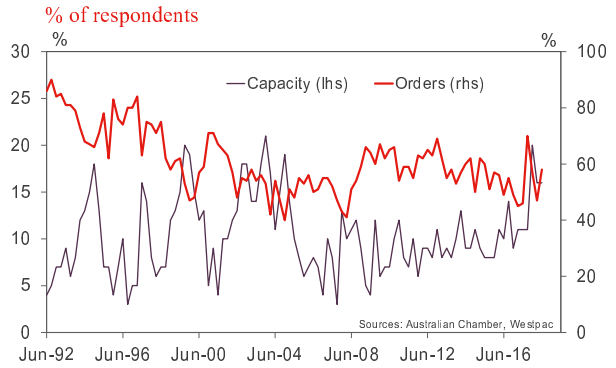
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Other results

Availability of labour & finance

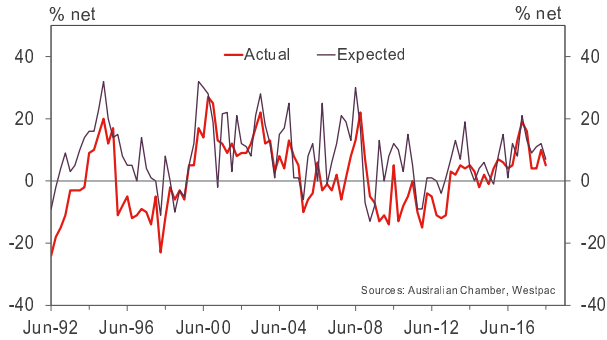


Key factor limiting production

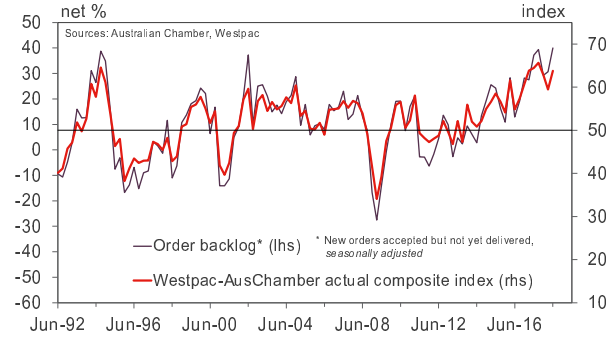


Average selling prices

Actual & expected

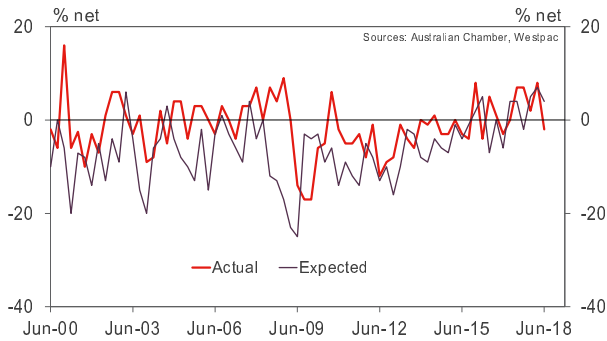


Order backlog & actual conditions



Stocks of finished goods

Actual & expected



Factors limiting production

	Q4 2017	Q1 2018	Q2 2018
Orders (%)	57	47	58
Capacity (%)	20	16	16
Labour (%)	3	3	4
Finance (%)	2	4	3
Materials (%)	2	3	0
Other (%)	12	21	8
None (%)	4	6	11

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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	39	59	2

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

Net balance	Above Normal	Normal	Below Normal
-2	12	74	14

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

None	11	Orders	58
Material	0	Finance	3
Labour	4	Capacity	16
Other	8		

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?	-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?	7	14	79	7
(b) on plant & machinery?	22	29	64	7

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	-2	5	88	7	6	12	82	6
7. Overtime worked	35	45	45	10	40	47	46	7
8. All new orders received	34	48	38	14	46	54	38	8
9. Orders accepted but not yet delivered	19	29	61	10	20	31	58	11
10. Output	38	46	46	8	37	50	37	13
11. Average costs per unit of output	32	37	58	5	15	19	77	4
12. Average selling prices	5	8	89	3	7	14	79	7
13. Export deliveries	3	6	91	3	5	6	93	1
14. Stock of raw materials	2	10	82	8	-6	4	86	10
15. Stocks of finished goods	-2	8	82	10	4	12	80	8

Summary of results *(not seasonally adjusted)*

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

(a) Improve?	37
(b) Remain unchanged?	52
(c) Decline?	11
Net balance	26

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?	32
(b) Same?	62
(c) Less?	6
Net balance	26

A. Industry profile of survey:

	(% of respondents)
Food, beverages, tobacco	15
Textiles, fabrics, floor coverings, felt, canvas, rope	6
Clothing, footwear	7
Wood, wood products, furniture	2
Paper, paper products, printing	8
Chemicals, paints, pharmaceuticals, soaps, cosmetics petroleum & coal products	10
Non-metallic mineral products: glass, pottery, cement bricks	4
Basic metal products: processing, smelting, refining, pipes & tubes	2
Fabricated metal products: structural & sheet metal, coating & finishing, wire, springs, hand tools	15
Transport equipment: motor vehicles & parts, excluding repairs, rail, ships, aircraft, including repairs	5
Other machinery & equipment: electrical, industrial scientific, photographic	18
Miscellaneous: including manufacturers of leather, plastic & rubber, sporting equipment, jewellery	8

B. How many employees are covered by this return?

	1-100	101-200	201-1000	Over 1000
	54	10	14	22

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

	WA	SA	VIC	NSW/ACT	QLD	TAS
	10	9	18	48	11	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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Things you should know.

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