

# Australian Chamber–Westpac Survey of Industrial Trends

Australian Chamber of Commerce and Industry & Westpac Banking Corporation

## 228<sup>th</sup> report September 2018 (survey conducted 26 July to 3 September 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 rose in September 2018 to 66.5 from 64.1 in June. The increase in September consolidates on June's bounce from two quarters of easing to 59.5 in March.
- The well above average reading for the Composite index reflects strength in new orders, output, employment, overtime, and backlog. The Australian economy has seen a period of strong expansion in the year to June 2018 with annual output growth of 3.4%, which is the fastest pace since 2012.
- Manufacturing is benefitting from: a strong upswing in non-residential construction, in particular public infrastructure investment with state governments continuing to add new projects to the pipeline, as well as robust external demand supported by a relatively low Australian dollar. More recently, the drought in New South Wales and Queensland is presenting challenges for the agriculture sector which has flow-on effects for some manufacturing firms.
- The uptrend in exports has continued at a moderate pace after stumbling back in 2016. A relatively low level of the Australian dollar is boosting international competitiveness, although overall global conditions have softened amidst uncertainty surrounding trade policy. Export expectations are for a similarly positive level over the next three months.
- Expectations are positive, centred on new orders, output, backlog, overtime and to a lesser extent, employment. The expected Composite fell to 61.1 from 66.7 in June. It is likely that some impact from the drought has been factored into firms' expectations. A net 22% of firms anticipate that the general business situation will improve over the next six months. This is down from a net 37% in June and is possibly affected by the recent increase in uncertainty regarding public policy, though note a still 89% of firms expect the general business situation to improve or remain unchanged.
- Equipment investment intentions of firms 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 21% of firms plan to increase equipment investment over the next year. Building intentions are solid, a net 7% of respondents intend to increase building investment over the next year, unchanged from June.
- The survey's Labour Market Composite, which broadly tracks economy-wide jobs, is at 58.0. The index correctly foreshadowed the acceleration in employment through 2017 and identified the turning point to softer momentum in 2018. The current positive level of the index suggests continued resilience in employment growth following the softer start to 2018.

# Contents

Key survey results	4
The business cycle & economic outlook	5
Activity & orders	6
Investment & profitability	7
The labour market	8
Prices & inflation	9
Other results	10
Summary of survey results	11

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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 228<sup>th</sup> consecutive survey was closed on 3rd September 2018.

A total of **297** 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 November/December 2018.

# Key survey results

## Westpac–AusChamber Composites *(seasonally adjusted)*

	Q2 2018	Q3 2018
Actual – composite index	64.1	66.5
Expected – composite index	66.7	61.1

- The Westpac-AusChamber Actual Composite Index rose to 66.5 in September from 64.1 in June. The index has now recovered all of the softening seen through December and March.
- The Composite is at a well above par level with strength seen across new orders, output, employment, backlog and overtime.
- Non-residential construction, in particular public infrastructure investment, continues to drive growth with new projects being added to the pipeline.
- The Expected Composite fell to 61.1 from 66.8 in June. The drought is presenting challenges for agriculture, and while food & beverage manufacturing has held up to date, flow-on effects are imminent.

## Westpac–AusChamber Labour Market Composite

	Q2 2018	Q3 2018
Net balance	57.4	58.0

- 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 increased to 58.0 from 57.4.
- The Index correctly led the uplift in employment in 2017. Official data report that employment growth was 3.2% in 2017 - an unsustainable quick pace.
- The positive level of the index suggests continued resilience in employment growth following the softer start to 2018. Currently, employment growth is tracking at 1.7% year to date annualised.

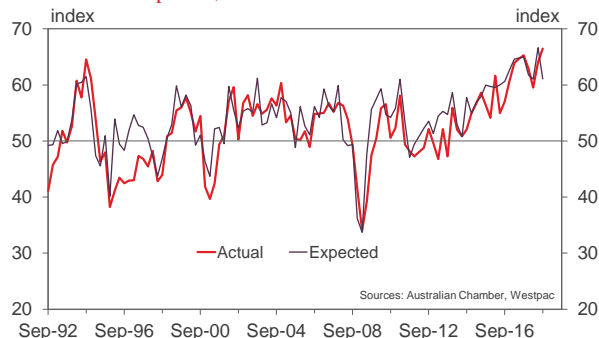
## General business situation

	Q2 2018	Q3 2018
Net balance	37	22

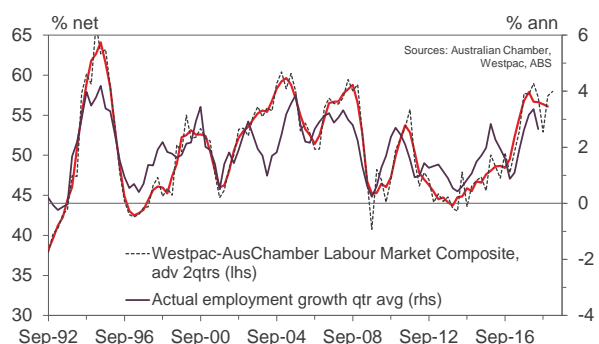
- Manufacturing firms are positive on the general business environment, though sentiment softened in the September quarter. A net 22% of respondents expect the general business situation to improve over the next six months, compared to a net 37% in June. The move lower is in line with that of the Expected Composite.
- The June survey took place post the May Federal Budget and manufacturers' continued optimism suggested that this year's policy reinforced the mood.
- Since then, public policy uncertainty has increased with the change of Prime Minister occurring during the time of this September quarter survey.
- In addition, global uncertainty is also elevated due to the ongoing negotiations surrounding trade.

## Westpac-AusChamber Composite indexes

Actual & expected, sa

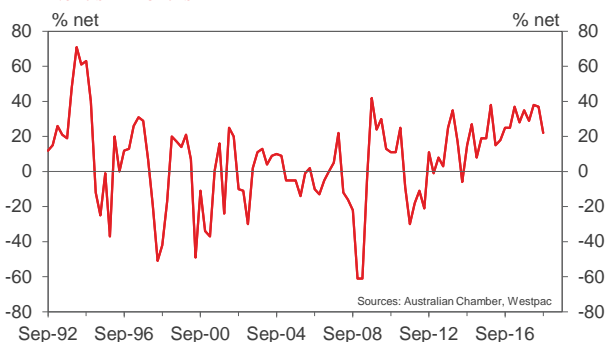


## Employment: momentum has peaked



## 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 activity has been mainly driven by sectors outside of the household sector.
- Non-residential construction, in particular public infrastructure investment, has been the primary source of demand. In addition, the food and beverages sector is growing with external demand supported by the relatively low level of the AUD.
- The ABS Q2 national accounts showed manufacturing output had a softer quarter, down 1.5%, partly retracing Q1's 2.3% gain. But annual growth remains positive with 2017 marking the first calendar year of expansion since 2011.

## Australian & World manufacturing surveys

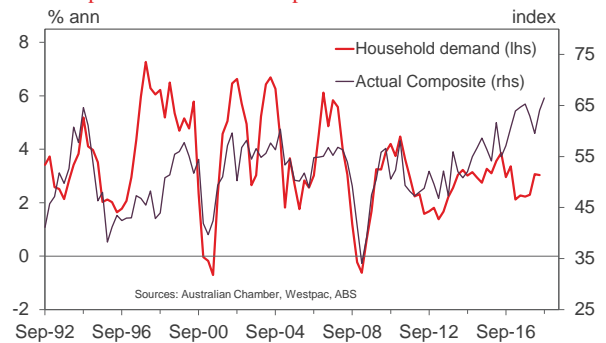
- Global and Australian manufacturing cycles tend to be synchronised, particularly at major turning points.
- Historically, the Westpac-AusChamber Actual Composite had moved broadly in line with global manufacturing conditions.
- However, since 2014, the Composite has deviated to the upside. In part this reflects Australian outperformance as easier monetary policy led to an upswing in homebuilding, but it also reflected the transitional effect of exiting firms. Of late, public infrastructure investment is boosting activity.
- Global manufacturing expanded in 2017 mirroring the synchronised uplift in growth seen around the world. In 2018, activity has slowed and diverged across nations. In addition, sentiment has been affected by concerns over trade policy.

## Manufacturing & business investment

- The AusChamber-Westpac survey has a solid track record of predicting equipment investment from the manufacturing sector.
- Manufacturing firms are intending to expand investment over the next year. In September, a net 21% of respondents are planning to increase plant and equipment investment over the next twelve months.
- The ABS capex survey confirms the strength in manufacturing equipment investment. The 2017/18 financial year saw a 7.9% rise in real manufacturing equipment investment which is the largest increase since the GFC. That is in part catch-up from a broadly flat 2016/17 but follows a solid 3.0% increase in 2015/16.

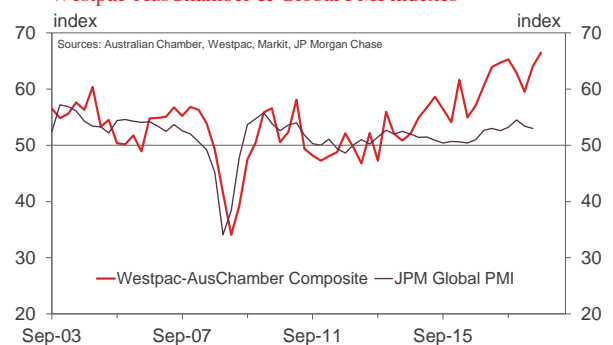
## Manufacturing & the business cycle

### Westpac-AusChamber Composite & household demand



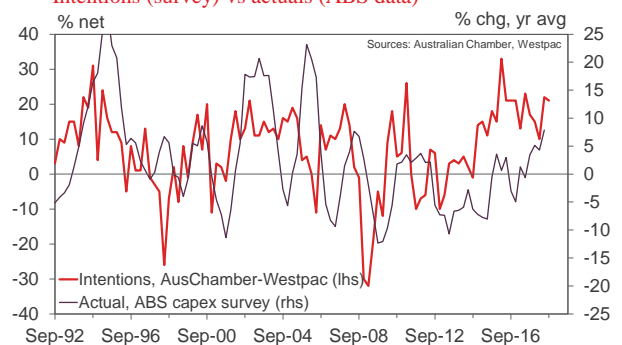
## Australian & World manufacturing surveys

### Westpac-AusChamber & Global PMI indexes



## Manufacturing equipment investment

### Intentions (survey) vs actuals (ABS data)



# Activity & orders

## Output *(seasonally adjusted)*

	Q2 2018	Q3 2018
Actual - net balance	40	43
Expected - net balance	38	27

- Manufacturing output has been in expansion for seventeen consecutive quarters. In September, a net 43% of respondents indicated higher output.
- The uptrend emerged in 2014 and has maintained a strong pace over the past few years, despite a short-lived slowing in the first half 2018.
- Expectations point to a period of deceleration in the next quarter with a net 27% of firms expecting output to increase in the next three months compared to the net 38% in June.

## New orders *(seasonally adjusted)*

	Q2 2018	Q3 2018
Actual - net balance	38	42
Expected - net balance	49	31

- Higher new orders are driving the expansion in output. A net 42% of firms reported an increase in new orders in September.
- Similar to output, new orders expectations declined. A net 31% of respondents anticipate that new orders will increase in the next three months. That is back to a similar net percentage as March after the brief lift higher to a net 49% in June.
- While many of the manufacturing growth drivers remain intact, namely public infrastructure, the drought has adversely affected conditions in the agriculture sector. The difficulties faced here will have spill-over effects, particularly for the food and beverages industry.

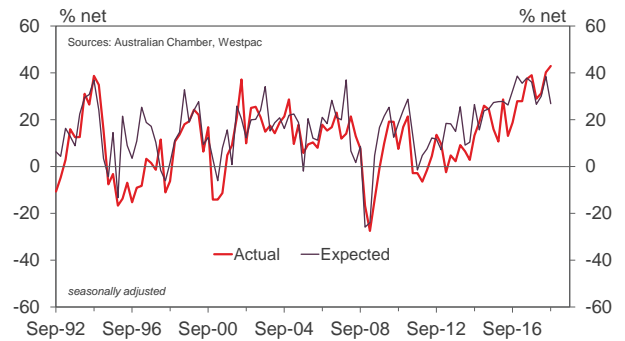
## Exports

	Q2 2018	Q3 2018
Actual - net balance	3	6
Expected - net balance	5	6

- Exports are continuing along a moderate uptrend. In September, a net 6% of respondents indicated that exports increased.
- While the Australian dollar has declined in the past few months, so has global growth momentum with trade uncertainty also elevated. It would appear that the boost to competitiveness has offset the slower pace of global demand as Australian manufacturing firms continue to report expanding exports.
- Export expectations indicate a net 6% of respondents are anticipating higher exports in the next three months.

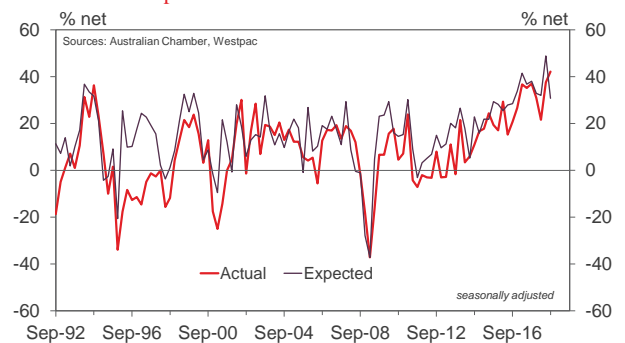
## Output growth

### Actual & expected



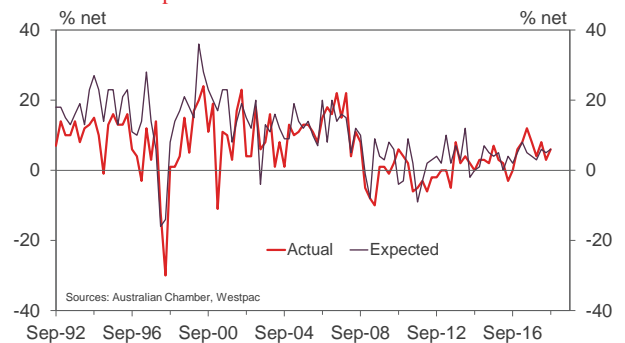
## New orders

### Actual & expected



## Export deliveries

### Actual & expected



# Investment & profitability

## Investment intentions

	Q2 2018	Q3 2018
Plant & Equipment - net balance	22	21
Building - net balance	7	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 September, a net 21% of respondents are planning to increase plant and equipment investment over the next twelve months. Official ABS surveys indicate that the 2017/18 financial year was the strongest year for real manufacturing equipment investment growth since the GFC.
- Building investment intentions are also positive. In September, a net 7% of respondents expect to increase building in the next twelve months.

## Capacity utilisation

	Q2 2018	Q3 2018
Net balance	-2	-1

- Capacity utilisation remains at an elevated level following the uplift seen from late 2013 to late 2015. Since then, capacity utilisation has gradually trended up with 88% at or above normal capacity levels.
- The number of firms operating above normal capacity was less than the number of firms below normal capacity by a net 1%. The share operating at normal capacity is high at around three quarters.
- A net 61% of firms indicate that the single factor most limiting their ability to increase production is orders. Yet, a still 14% indicate that their single factor is capacity which suggests that equipment investment should remain supported over the period ahead.

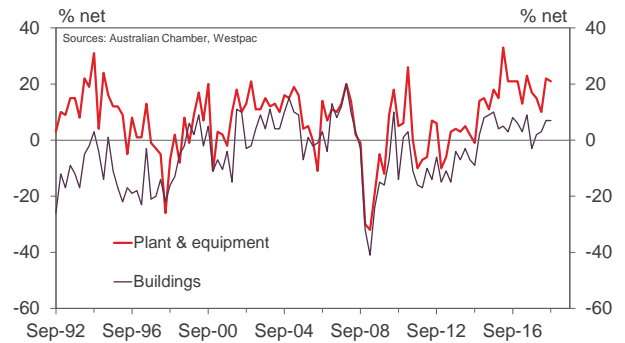
## Profit expectations

	Q2 2018	Q3 2018
Net balance	26	30

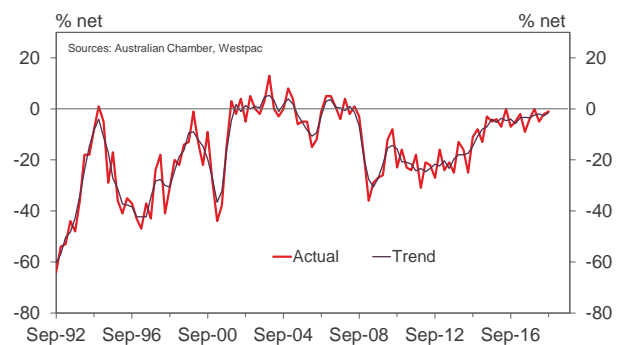
- Manufacturing firms' profitability expectations continue to be solid as output and new orders expand.
- Expectations firmed again in September after June's recovery from a dip lower than that ended in March.
- In September, a net 30% of respondents are anticipating that profitability will increase over the next twelve months.
- Official data confirms that profitability has improved in the manufacturing sector. The ABS Business Indicators survey reports that manufacturing gross operating profits increased by 7.2% in the 2017/18 financial year.

## Investment intentions

### Next twelve months

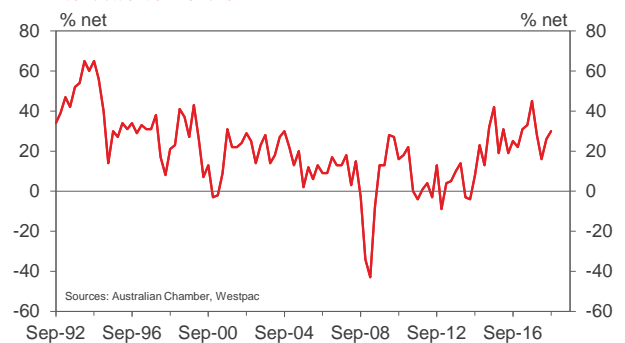


## Capacity utilisation



## Profit expectations

### Next twelve months



# The labour market

## Numbers employed *(seasonally adjusted)*

	Q2 2018	Q3 2018
Actual - net balance	-1	10
Expected - net balance	7	4

- Manufacturing employment bounced back in September as heralded by the lift in employment expectations in the June survey.
- A net 10% of firms indicated that they increased their workforce in September. Firms are responding to higher output and the increased use of overtime by hiring more employees.
- A net 4% of respondents expect to expand their workforce in the next three months. It is likely that firms' reduced expectations for output have contributed to greater caution on hiring practices. The recent bout of public policy uncertainty, as well as other global issues, may also be factors.

## Overtime worked *(seasonally adjusted)*

	Q2 2018	Q3 2018
Actual - net balance	38	40
Expected - net balance	41	32

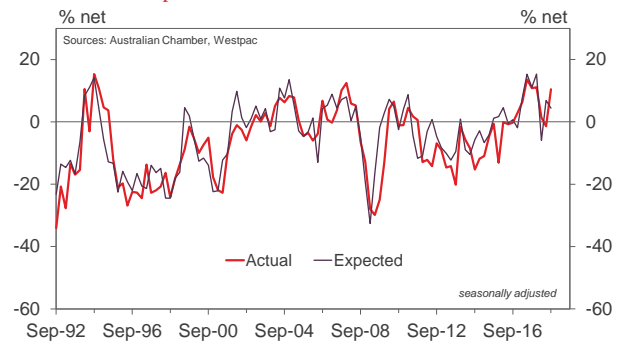
- The increased use of overtime continues to be widely reported, consistent with the higher levels of output that we have been seeing.
- In September, a net 40% of respondents indicated that they increased overtime. Expectations for the coming quarter are also high, albeit slightly lower than that reported in June. A net 32% of respondents anticipate an increased use of overtime over the next three months.
- A high use of overtime was historically not the norm in the manufacturing sector. But with output expectations lower and added uncertainty around policy, firms are opting for a wait-and-see approach before making longer term commitments.

## Difficulty of finding labour *(seasonally adjusted)*

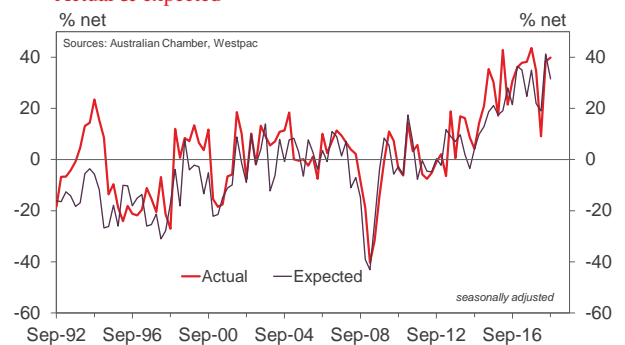
	Q2 2018	Q3 2018
Net balance	2	8

- 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 8% of respondents indicated that labour was harder to find in September. This is an increase from a net 2% in June but still lower than the net 10% in March.
- Official ABS data has showed the pace of employment growth slowing in 2018 to a 1.7% annualised year to date pace. However, with growth in labour force participation more muted, the unemployment rate has ticked lower to 5.3%, the lowest level in five years.

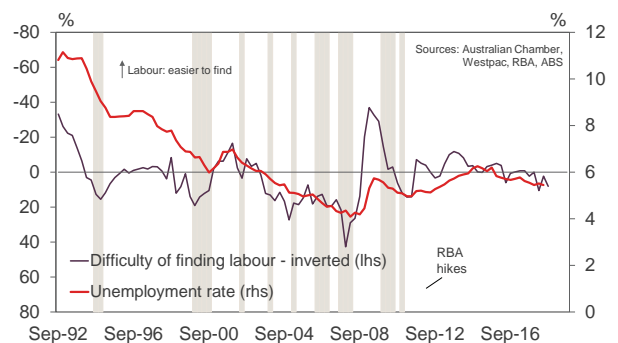
## Numbers employed Actual & expected



## Overtime worked Actual & expected



## Labour market tightness



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# Prices & inflation

## Average unit costs

	Q2 2018	Q3 2018
Actual - net balance	32	25
Expected - net balance	15	19

- 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 remains prescient with a net 25% of firms reporting that unit costs increased in September.
- Expectations of coming cost increases are also above average. A net 19% of respondents expect that unit costs will increase over the next three months.
- Electricity costs and a general rise in commodity prices have been front of mind for most firms. Now in addition, the drought in the eastern states will also add to cost pressures as well as the lower Australian dollar increasing import costs.

## Average selling prices

	Q2 2018	Q3 2018
Actual - net balance	5	17
Expected - net balance	7	11

- Price increases have become more prominent since mid 2013, in contrast to the lack of pricing power which was the norm prior to the GFC.
- However, despite the lift in input costs, pass through to selling prices have been to a lesser extent. A net 17% of firms reported increased prices in September, up from a net 5% in June.
- Expectations are more moderate with a net 11% of respondents indicating higher selling prices in the next three months. This is only slightly higher than the net 7% in June.

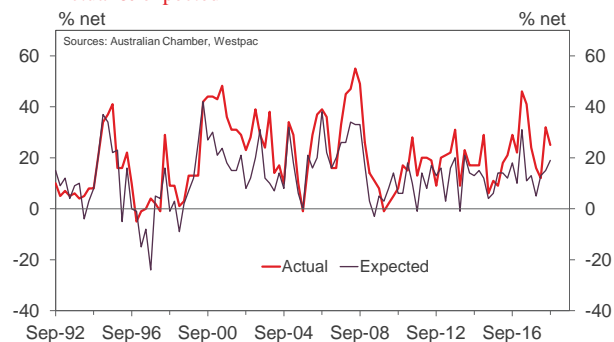
## Manufacturing wages

	Q2 2018	Q3 2018
Net balance	26	28

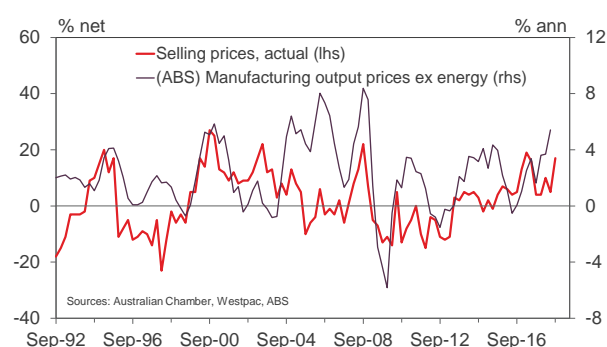
- The survey indicates that manufacturing wages growth will lift in the year ahead. A net 28% of firms in September expect that their next wage bill will deliver an outcome above the last.
- The Fair Work Commission opted for an above average 3.5% lift in award wages for 2018/19 following the 3.3% increase for 2017/18.
- The latest wage price index release showed annual manufacturing wages growth maintaining a pace of just above 2%, a little above the lows of 2016. The AusChamber-Westpac survey suggests that manufacturing wages growth should resume a nascent uptrend over the next few quarters.

## Average unit costs

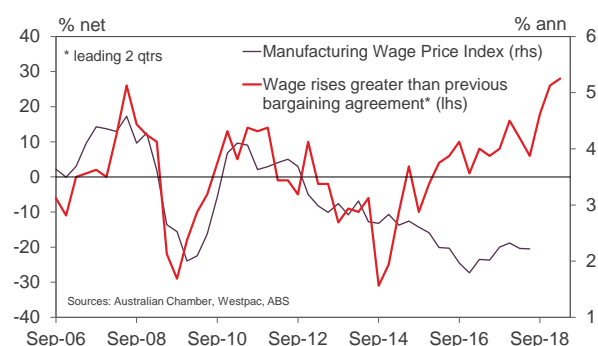
### Actual & expected



## Manufacturing upstream price pressures



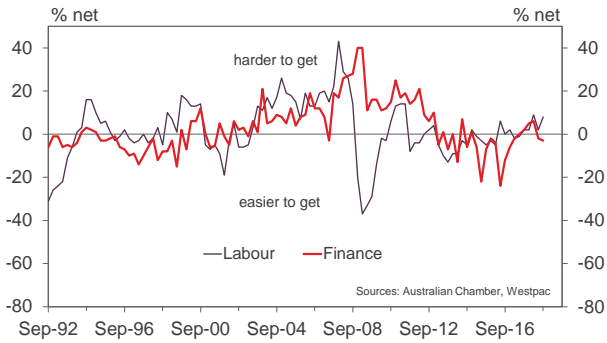
## Manufacturing wage growth



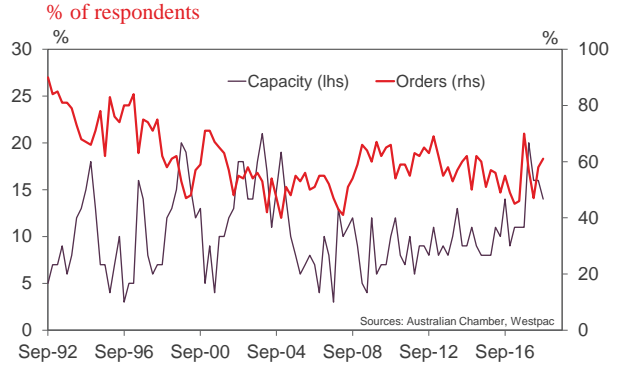


# Other results

## Availability of labour & finance

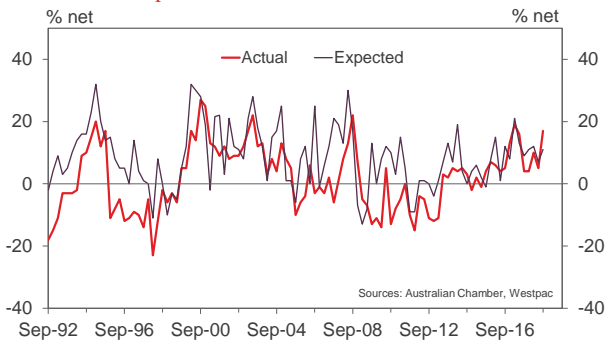


## Key factor limiting production

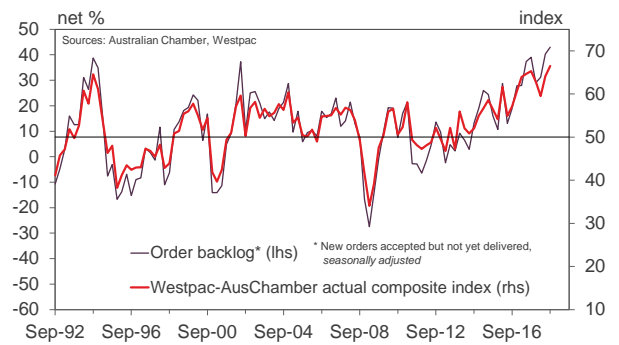


## Average selling prices

### Actual & expected

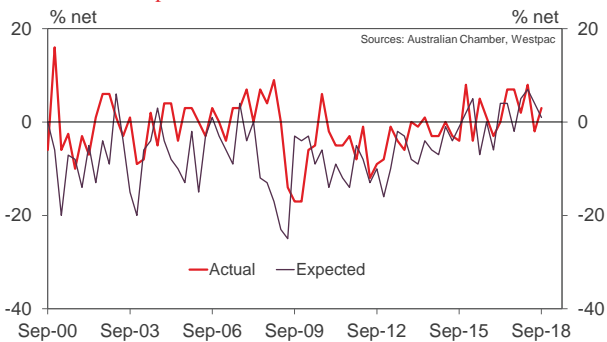


## Order backlog & actual conditions



## Stocks of finished goods

### Actual & expected



## Factors limiting production

	Q1 2018	Q2 2018	Q3 2018
Orders (%)	47	58	61
Capacity (%)	16	16	14
Labour (%)	3	4	4
Finance (%)	4	3	5
Materials (%)	3	0	1
Other (%)	21	8	10
None (%)	6	11	5

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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
22	33	56	11

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

Net balance	Above Normal	Normal	Below Normal
-1	11	77	12

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

None	5	Orders	61
Material	1	Finance	5
Labour	4	Capacity	14
Other	10		

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?	8	9	90	1
(b) finance?	-3	3	91	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	15	77	8
(b) on plant & machinery?	21	28	65	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	13	14	85	1	8	11	86	3
7. Overtime worked	39	47	45	8	41	43	55	2
8. All new orders received	38	48	42	10	38	45	48	7
9. Orders accepted but not yet delivered	22	28	66	6	28	31	66	3
10. Output	41	48	45	7	36	43	50	7
11. Average costs per unit of output	25	30	65	5	19	22	75	3
12. Average selling prices	17	19	79	2	11	13	85	2
13. Export deliveries	6	8	90	2	6	7	92	1
14. Stock of raw materials	0	7	86	7	-3	4	89	7
15. Stocks of finished goods	3	10	83	7	1	8	85	7

# Summary of results (not seasonally adjusted)

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

(a) Improve?	39
(b) Remain unchanged?	52
(c) Decline?	9
<b>Net balance</b>	<b>28</b>

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?	31
(b) Same?	66
(c) Less?	3
<b>Net balance</b>	<b>28</b>

A. Industry profile of survey:

	(% of respondents)
Food, beverages, tobacco	16
Textiles, fabrics, floor coverings, felt, canvas, rope	5
Clothing, footwear	5
Wood, wood products, furniture	3
Paper, paper products, printing	5
Chemicals, paints, pharmaceuticals, soaps, cosmetics petroleum & coal products	13
Non-metallic mineral products: glass, pottery, cement bricks	4
Basic metal products: processing, smelting, refining, pipes & tubes	3
Fabricated metal products: structural & sheet metal, coating & finishing, wire, springs, hand tools	14
Transport equipment: motor vehicles & parts, excluding repairs, rail, ships, aircraft, including repairs	4
Other machinery & equipment: electrical, industrial scientific, photographic	17
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
52	10	16	22

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

WA	SA	VIC	NSW/ACT	QLD	TAS
9	12	18	46	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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