Australian Chamber–Westpac Survey of Industrial Trends

Australian Chamber of Commerce and Industry & Westpac Banking Corporation

236th report September 2020 (survey conducted 3 August to 1 September 2020)

- 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 improved to 42.4 in the September quarter after falling dramatically to 24.0 in the June quarter associated with the initial lock-down in response to covid. The index remains well below its pre-covid level of 56 at the end of 2019.
- With the activity index still sub-50, this suggests conditions are contracting, but at a much slower rate. Of note, new orders and output are declining at a slower pace.
- The covid global pandemic and the measures to combat the virus have had a dramatic impact on the Australian economy - which slumped into recession in 2020 for the first time in 29 years. The emerging rebound from the initial lock-down experienced a set-back, with Victoria going into a second lock-down. The manufacturing sector has been greatly impacted by the disruptions and the downturn.
- As with the broader economy, within this overall weak picture, conditions in the manufacturing industry are mixed across sectors. The downturn in construction, particularly residential, has weighed heavily on metals manufacturers. However, the unprecedented conditions presented unique opportunities for certain segments - with demand soaring for medical equipment and disinfectants.
- Respondents' expectations around their own businesses have been marked lower, impacted by the set-backs in Victoria. The Expected Composite slipped to 44.1 in September, down from 50.5 in June, pointing to an expected soft end to the 2020 year.
- Around the general outlook, sentiment amongst manufacturers is downbeat, shaken by the challenging second lock-down in Victoria. A net 18% of respondents expect the general business situation to deteriorate over the next six months, little changed from a net 22% in June.
- Exports stabilised in the September quarter and expectations are mildy positive, supported by the progressive re-opening of the global economy.
- While the latest readings are generally an improvement on the extreme lows of the June quarter, the covid-driven economic downturn continues to have a significant impact on the manufacturing sector. Profit expectations are weak at -35, albeit up from -60 in the June quarter. Investment expectations are also weak, with a net 16% of respondents planning to reduce equipment investment over the next year.
- The survey's Labour Market Composite, which broadly tracks economy-wide employment growth, remains weak, at 34.3, albeit up from 29.4 in June. The index correctly foreshadowed recent cycles - the uplift in employment in 2017 and the slowing from 2018. The current reading implies that employment will remain at weak levels over coming quarters.

Contents

The Survey of Industrial Trends produced by the Australian Chamber of Commerce and Industry & Westpac Banking Corporation is a quarterly publication.

Enquiries
Economics, Westpac Banking Corporation, ph (61–2) 8254 8720
Eugene Bajkowski OAM, Consulting Economist, Australian Chamber of Commerce and Industry, ph (61–2) 6249 6128

Editors
Andrew Hanlan, Senior Economist, Westpac Banking Corporation
Josephine Tay, Westpac Banking Corporation
Eugene Bajkowski OAM, Consulting Economist, Australian Chamber of Commerce and Industry
Miranda Herron, Senior Consultant, Australian Chamber of Commerce and Industry

Email: economics@westpac.com.au

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 236th consecutive survey was closed on 1 September 2020.

A total of **231** 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 and December 2020.

Key survey results

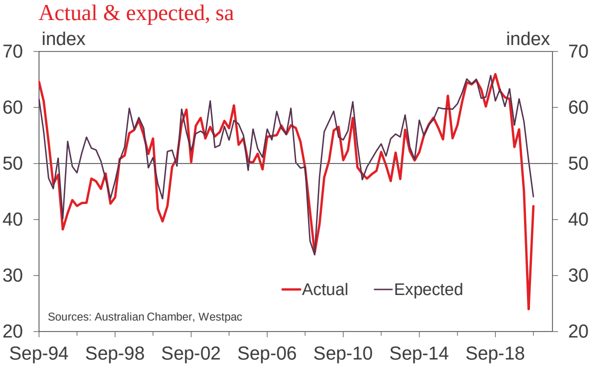
Westpac–AusChamber Composites *(seasonally adjusted)*

	Q2 2020	Q3 2020
Actual – composite index	24.0	42.4
Expected – composite index	50.5	44.1

- The Westpac–AusChamber Actual Composite improved to 42.4 in the September quarter after falling dramatically to 24.0 in June on the initial lock-down nationally in response to covid.
- With the reading still sub-50, this suggests conditions are contracting, but at a much slower rate. Of note, new orders and output are declining at a slower pace.
- The Expected composite weakened, slipping below 50, to 44.1 from 50.5. Earlier expectations for a quick rebound have been reassessed.
- Victoria's second lock-down was a key development, denting conditions in Q3 and delaying the recovery.

Westpac-AusChamber Composite indexes

Actual & expected, sa

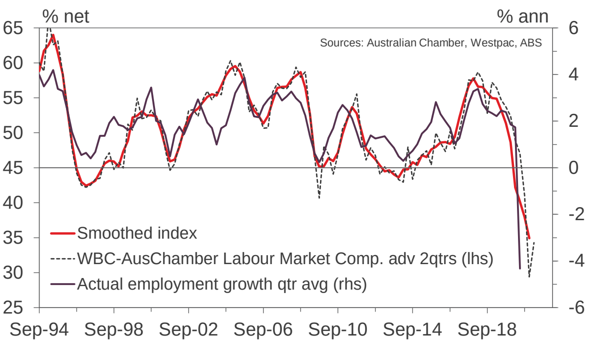


Westpac–AusChamber Labour Market Composite

	Q2 2020	Q3 2020
Composite index	29.4	34.3

- 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 correctly foreshadowed recent cycles - the uplift in employment in 2017, then the slowing from 2018.
- In 2020, the Composite plunged to 29.4 in the June quarter, lifting to a still weak 34.3 in September.
- Employment plunged during this recession as the economy went through a partial lock-down. Official data reports job levels in the June quarter 4.3% below a year earlier.
- The survey suggests that employment will remain at weak levels over coming quarters.

Employment: hit by covid recession



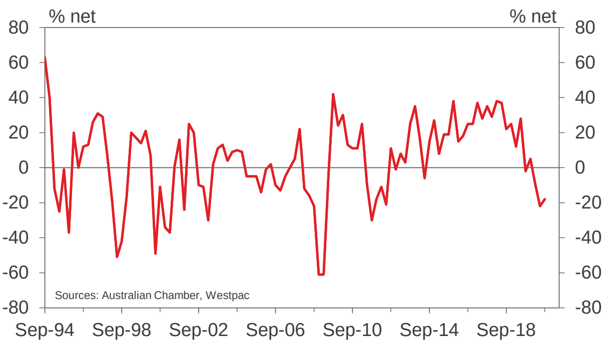
General business situation

	Q2 2020	Q3 2020
Net balance	–22	–18

- Manufacturing sentiment has been shaken by the covid crisis.
- First from the initial restrictions and initial lock-down nationally and more recently after the second wave of infections in Victoria.
- During the September quarter, a net 18% of respondents expect the general business situation to worsen over the next six months.
- That is only a slight improvement on the June reading, a shift of 4%.
- This is likely due to the high degree of uncertainty about further lock-down restrictions and the challenging environment more generally.

General business situation

Next six months



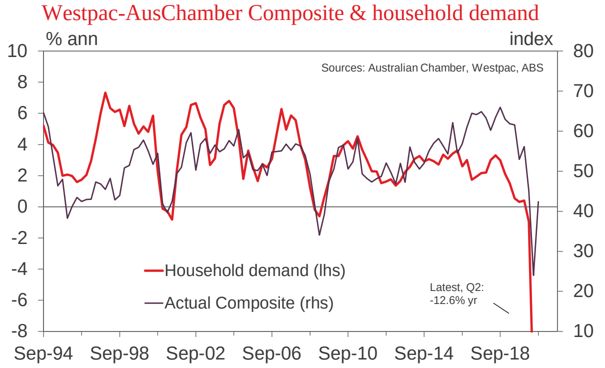
The business cycle & economic outlook

Manufacturing & the business cycle

- The Westpac–AusChamber Actual Composite index has a solid track record of predicting near-term domestic economic conditions and identifying turning points in the cycle.
- The covid pandemic and restrictions in response to the virus – notably temporary lock-downs – disrupted activity and impacted global supply chains. Consumer spending in Australia plunged by 12% in the June quarter, at the height of the national lock-down.
- The reopening of economies – with some set-backs – was the key development in the September quarter, leading to an improvement of conditions across the manufacturing sector.
- Interestingly, new conditions under social distancing measures have boosted some sectors through expenditure switching.

Manufacturing & the business cycle

Westpac-AusChamber Composite & household demand

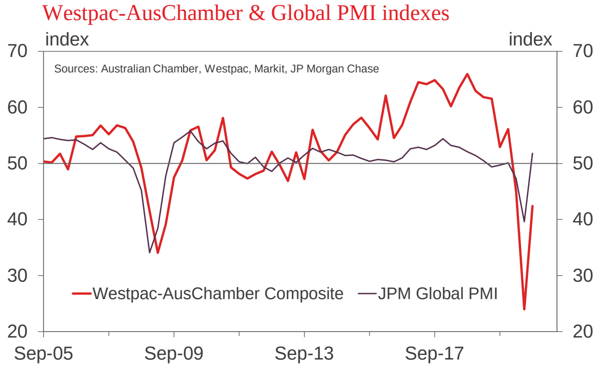


Australian & World manufacturing surveys

- Global and Australian manufacturing cycles tend to be synchronised, especially at major turning points.
- Historically, the Westpac–AusChamber Actual Composite has moved broadly in line with global manufacturing conditions.
- Although global manufacturing PMIs plummeted in April, they were among the few industries to experience an equally rapid comeback. They have since recovered to near pre-covid levels.
- China, with a significant manufacturing presence, has made a strong recovery. At its latest read the Caixin China PMI was 53.1, up from a low of 40.3.
- Both US and Eurozone manufacturing PMIs are sitting comfortably above the 50-threshold for expansion (56.0 and 51.7 respectively). This has been led by a pick up in output and new orders as economies reopen and business sentiment returns.

Australian & World manufacturing surveys

Westpac-AusChamber & Global PMI indexes

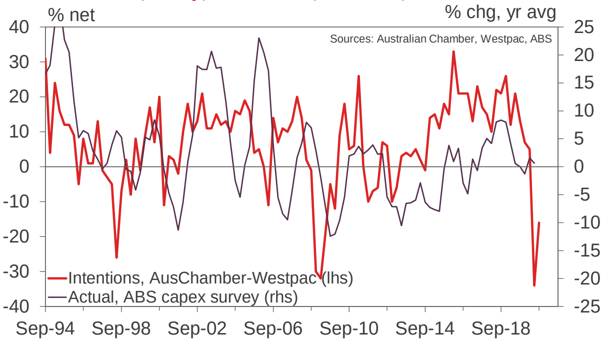


Manufacturing & business investment

- The AusChamber–Westpac survey has a solid track record of predicting equipment investment from the manufacturing sector.
- Manufacturing firms investment intentions are downbeat, with a net 16% planning to reduce plant and equipment investment over the next twelve months. While up from the extreme low of a net 34% in June, this is still well below pre-covid levels.
- The ABS capex survey also points to a weak investment outlook at a time of excess spare capacity and an uncertain outlook.
- In the June quarter ABS capex update, manufacturing investment plans for 2020/21 were 12% below the corresponding estimate a year earlier. This included equipment plans, -11% and building and structures intentions, -14%.

Manufacturing equipment investment

Intentions (survey) vs actuals (ABS data)



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.

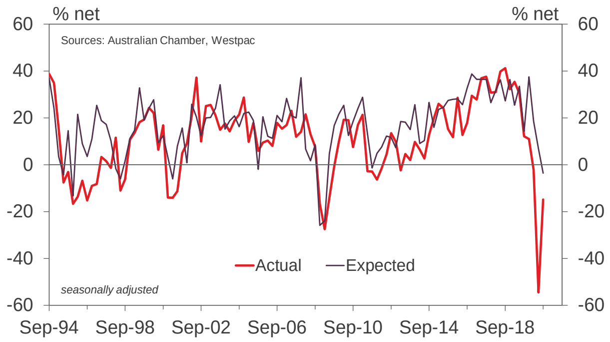
Activity & orders

Output *(seasonally adjusted)*

	Q2 2020	Q3 2020
Actual – net balance	–55	–15
Expected – net balance	7	–4

- Output is contracting but at a much slower rate, that is the key message from this update. A net 15% of firms indicated that output decreased in the September quarter, a significant improvement on the net 55% decline in June.
- The experience and performance by sectors and by states will have varied. Most notably, the re-opening of the economy is more advanced outside of Victoria.
- Earlier expectations for a quick snap back in conditions have been reassessed - arguably the exit path from the initial lock-down was always going to be a bumpy ride. A net 4% expect output to decline in Q4, in contrast to 3 months earlier, when 7% anticipated a rise.

Output growth
Actual & expected

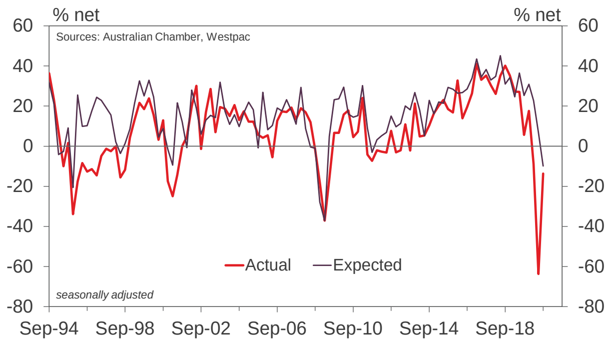


New orders *(seasonally adjusted)*

	Q2 2020	Q3 2020
Actual – net balance	–64	–14
Expected – net balance	7	–10

- Following a plunge in new orders in the June quarter, the rate of decline slowed appreciably in the September quarter as many businesses progressively began to reopen.
- A net 14% of respondents reported fewer new orders in September, a marked improvement on the net 64% who identified that new orders had decreased over June.
- Expectations have deteriorated, with respondents now anticipating a soft end to the 2020 year.
- A net 10% of firms expect new orders will fall in the coming quarter, in contrast to the June quarter where a net 7% expected new orders to rise.

New orders
Actual & expected

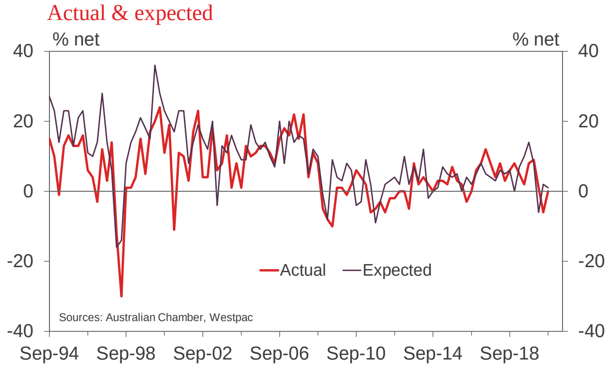


Exports

	Q2 2020	Q3 2020
Actual – net balance	–6	0
Expected – net balance	2	1

- Exports stabilised in the September quarter, in contrast to contracting conditions domestically.
- The number of exporters reporting a rise in orders in Q3 matched those reporting a fall. That is an improvement on the net 6 decline in the June quarter.
- The global economy, while still weak, rebounded from mid-year as restrictions were rolled back, thereby supporting global trade.
- Expectations are still mildly positive, with a net 1% expecting exports to rise in the final months of 2020.
- A potential concern is the exchange rate, with the Australian dollar moving back above US 70¢, buoyed by positive news on the global reopening.

Export deliveries
Actual & expected



Investment & profitability

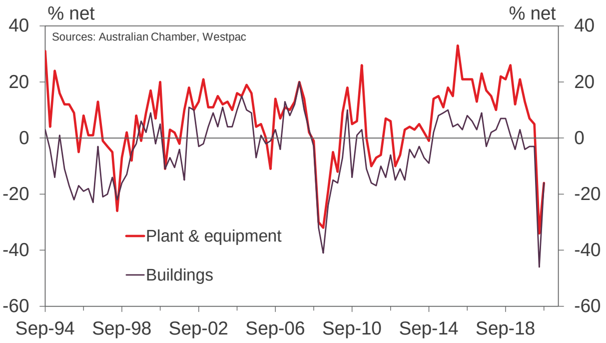
Investment intentions

	Q2 2020	Q3 2020
Plant & Equipment – net balance	–34	–16
Building – net balance	–46	–16

- Investment intentions are deeply negative, albeit up from the extreme lows of the June quarter.
- A net 16% of firms are intending to decrease plant and equipment investment over the next twelve months, an improvement on a net 34% in June.
- The economic recession and heightened uncertainty are major negatives for investment. The manufacturing sector now faces substantial excess capacity and profitability is under intense pressure.
- Building intentions are downbeat, with a net 16% of firms intending on reducing investment in buildings over the year ahead, albeit up materially from the net 46% three months ago.

Investment intentions

Next twelve months

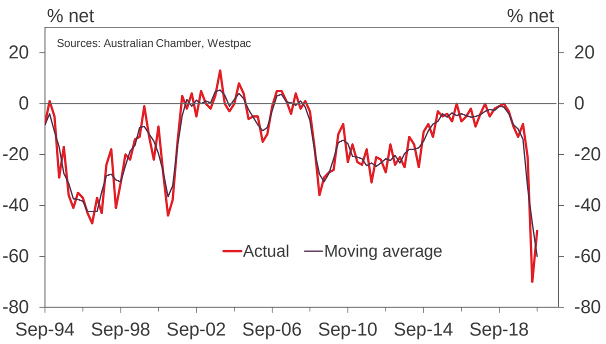


Capacity utilisation

	Q2 2020	Q3 2020
Net balance	–70	–50

- The recession of 2020 associated with the response to covid leaves the manufacturing sector and the economy more generally with considerable excess capacity.
- In the June quarter, capacity utilisation plunged to -70. The survey indicates a moderate improvement in capacity utilisation in the September quarter, as firms began to resume operations.
- A net 50% of firms indicated they were operating below capacity in September. Expressed differently, 39% of firms were at or above full capacity in September, up from a net 25% in June.
- Ongoing restrictions - such as social distancing requirements in the workplace - are impacting the ability of firms to operate normally.

Capacity utilisation



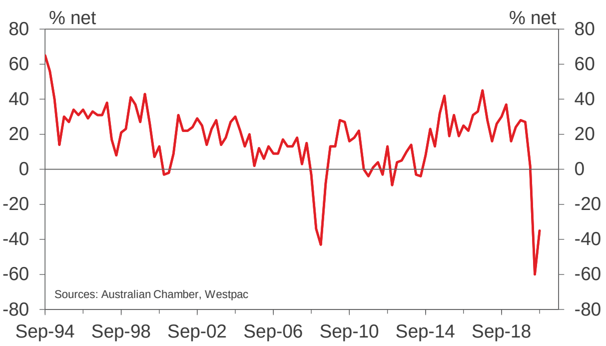
Profit expectations

	Q2 2020	Q3 2020
Net balance	-60	-35

- The profitability of the manufacturing sector has been hard hit by the covid recession.
- Manufacturers' profit expectations were deeply negative in the September quarter, albeit up from the extreme low of June.
- A net 35% of respondents expect profits to fall over the next year, up from a net 60% in June.
- The key negative is the plunge in revenue associated with the weaker demand. At the same time, costs continue to rise.

Profit expectations

Next twelve months

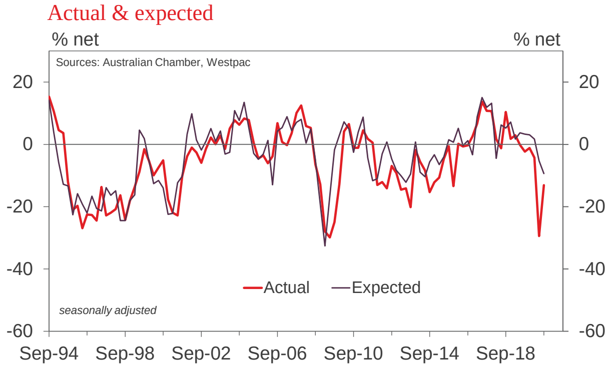


The labour market

Numbers employed *(seasonally adjusted)*

	Q2 2020	Q3 2020
Actual – net balance	–29	–13
Expected – net balance	–5	–9

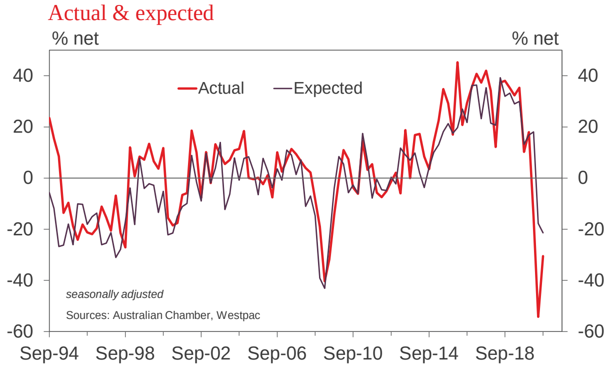
- Firms are having to materially adjust their business operations in response to the covid recession.
- This includes a scaling back of their workforce. The adjustment continued in the September quarter as output fell further, albeit declining at a slower rate.
- In this update, a net 13% of firms reported a reduction in employment over the quarter, following a net 29% decline in the June quarter.
- Expectations of future employment weakened, with a net 9% anticipating a decline in the coming three months, after a 5% in June. This is consistent with the deteriorating environment, impacted by Victoria's second lock-down.



Overtime worked *(seasonally adjusted)*

	Q2 2020	Q3 2020
Actual – net balance	–54	–30
Expected – net balance	–18	–21

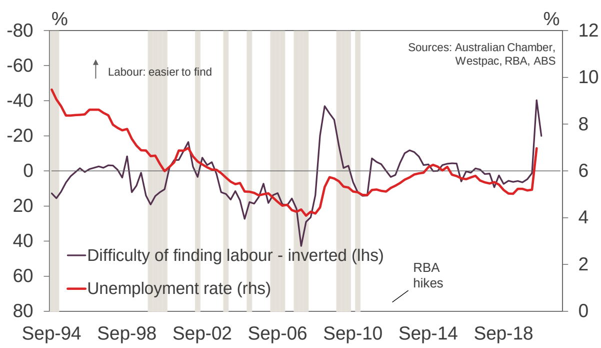
- Consistent with the material decline in production, the use of overtime has been greatly reduced.
- A net 30% of respondents indicated that they reduced overtime, up from a net 54% in June.
- The experience will vary across the manufacturing sector. Those who produced goods that were stockpiled, such as chemicals and food manufacturers, likely increased overtime to meet the spike in demand. However, conditions across more vulnerable sectors will have softened considerably.
- A net 21% of firms are expecting to reduce overtime over the next three months.



Difficulty of finding labour *(seasonally adjusted)*

	Q2 2020	Q3 2020
Net balance	–40	–20

- The survey provides insights into the tone of the overall labour market. Firms' views on the difficulty of finding labour broadly track shifts in the unemployment rate for the Australian economy.
- A net 20% of firms indicated labour was "easier to find" in September, an improvement on a net 40% in June. Whilst this points to considerable labour market slack, the survey is well above the extreme lows during the early 1980s and 1990s recessions, on both occasions falling below –60. Currently, the JobKeeper program is acting to dampen labour market stress.
- The covid recession has seen the unemployment rate jump from around 5.0% in February to 7.5% in July. Alternatively, if the participation rate had stayed at pre-covid levels, unemployment would be at 9.3%.



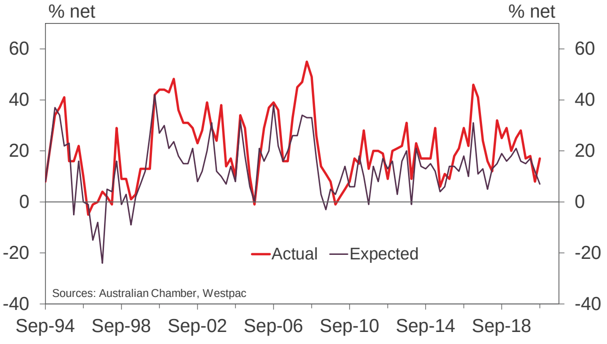
Prices & inflation

Average unit costs

	Q2 2020	Q3 2020
Actual – net balance	8	17
Expected – net balance	12	7

- In the years prior to covid, input cost inflation was a heightened concern for manufacturing firms - most notably around energy costs.
- Cost escalation is an ongoing issue - which is even more challenging during covid as revenues fall.
- The number of firms reporting an increase in costs rose to a net 17% in September, up from 8% in June.
- Crude oil prices sold-off sharply earlier in the year as covid hit. Subsequently, crude prices moved off their lows, contributing to the recent rise in units costs. That said, the key focus for many firms remains the cost of electricity.

Average unit costs
Actual & expected

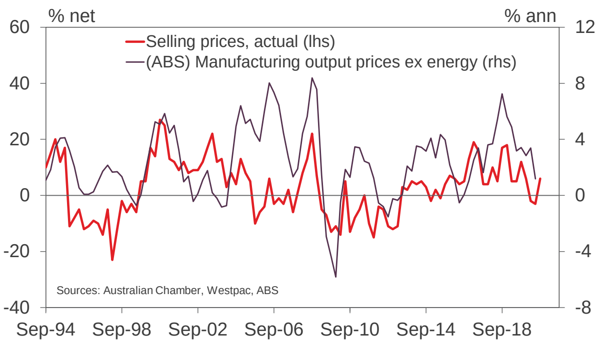


Average selling prices

	Q2 2020	Q3 2020
Actual – net balance	–3	6
Expected – net balance	2	5

- Selling price increases have typically been more moderate relative to the rise in average unit costs.
- This dynamic has continued during 2020.
- In the September quarter, a net 6% of respondents indicated they increased their prices and a net 5% expect to lift prices in the final months of 2020.
- By contrast, a net 17% reported a rise in costs during the June quarter.
- This lack of pricing power - understandable during the covid recession - reinforces the deterioration in profitability.

Manufacturing upstream price pressures

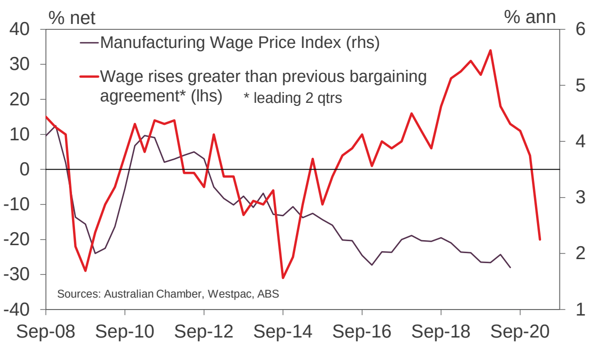


Manufacturing wages

	Q2 2020	Q3 2020
Net balance	4	–20

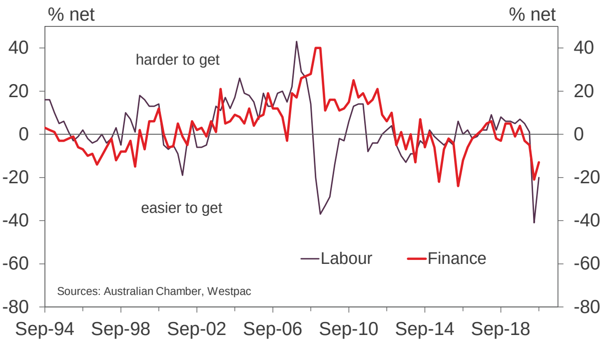
- The survey reports a sharp weakening in wage expectations associated with the unfolding recession - a trend that accelerated in September after Victoria re-entered lockdown.
- In September, a net 20% of respondents expect that their next wage deal will deliver an outcome below their last, down from a net 4% and 11% in the two previous quarters who expected higher outcomes.
- Official data shows that manufacturing wage inflation has been slowing since late 2018.
- More broadly, wage inflation has been soft across the entire economy and the RBA does not anticipate a pick-up until we approach full employment levels of around 4-4.5%.

Manufacturing wage growth



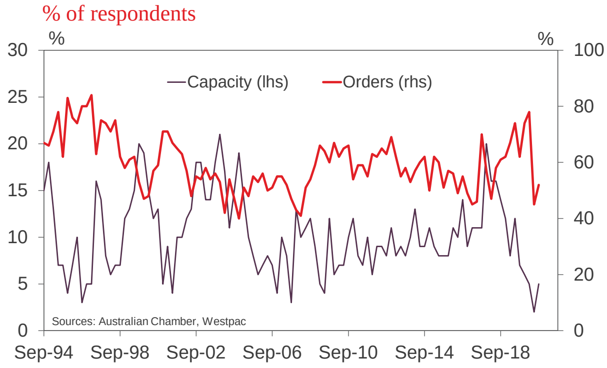
Other results

Availability of labour & finance



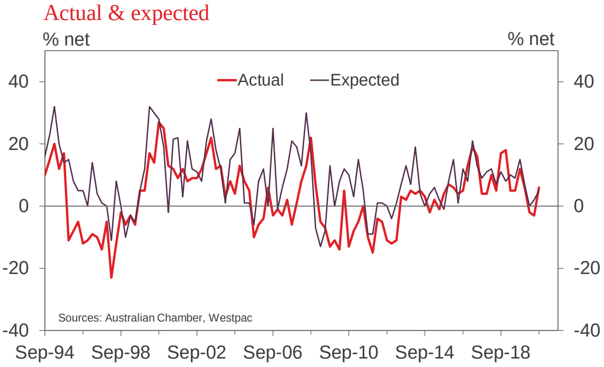
Key factor limiting production

% of respondents

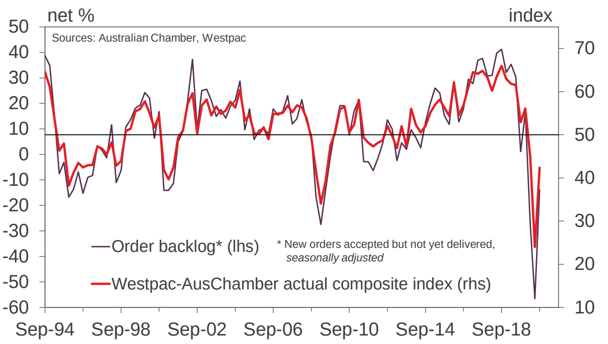


Average selling prices

Actual & expected

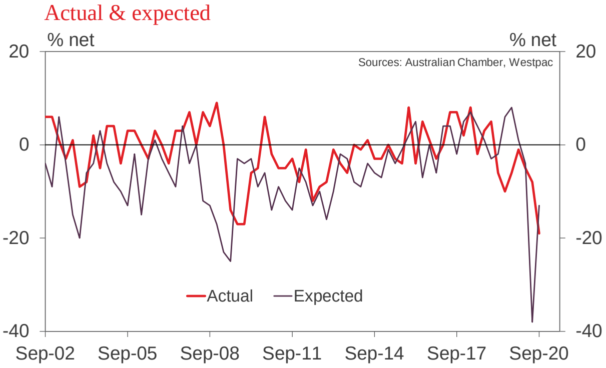


Order backlog & actual conditions



Stocks of finished goods

Actual & expected



Factors limiting production

	Q1 2020	Q2 2020	Q3 2020
Orders (%)	78	45	52
Capacity (%)	5	2	5
Labour (%)	6	4	3
Finance (%)	2	3	0
Materials (%)	1	2	4
Other (%)	7	44	36
None (%)	1	0	0

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
–18	13	56	31

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

Net balance	Above Normal	Normal	Below Normal
–50	11	28	61

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

None	0	Orders	52
Material	4	Finance	0
Labour	3	Capacity	5
Other	36		

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?	–20	5	70	25
(b)	finance?	–13	6	75	19

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?	–16	14	56	30
(b)	on plant & machinery?	–16	16	52	32

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	–11	9	71	20	–7	9	75	16
7.	Overtime worked	–30	12	46	42	16	14	56	30
8.	All new orders received	–15	23	39	38	–5	19	57	24
9.	Orders accepted but not yet delivered	–14	17	52	31	–15	10	65	25
10.	Output	–15	23	39	38	3	22	59	19
11.	Average costs per unit of output	17	20	77	3	7	10	87	3
12.	Average selling prices	6	7	92	1	5	6	93	1
13.	Export deliveries	0	6	88	6	1	5	91	4
14.	Stock of raw materials	–9	14	63	23	–9	7	77	16
15.	Stocks of finished goods	–19	14	53	33	–13	10	67	23

Summary of results *(not seasonally adjusted)*

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

(a) Improve?	20
(b) Remain unchanged?	25
(c) Decline?	55
Net balance	**-35**

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?	10
(b) Same?	60
(c) Less?	30
Net balance	**-20**

A. Industry profile of survey:

	(% of respondents)
Food, beverages, tobacco	14
Textiles, fabrics, floor coverings, felt, canvas, rope	4
Clothing, footwear	3
Wood, wood products, furniture	3
Paper, paper products, printing	8
Chemicals, paints, pharmaceuticals, soaps, cosmetics petroleum & coal products	10
Non-metallic mineral products: glass, pottery, cement bricks	7
Basic metal products: processing, smelting, refining, pipes & tubes	3
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	2
Other machinery & equipment: electrical, industrial scientific, photographic	23
Miscellaneous: including manufacturers of leather, plastic & rubber, sporting equipment, jewellery	7

B. How many employees are covered by this return?

1-100	101-200	201-1000	Over 1000
49	12	17	22

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

WA	SA	VIC	NSW/ACT	QLD	TAS
13	13	22	35	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.

This report was finalised on 9 September 2020
Publication enquiries, Economics, Telephone (61-2) 8254 8720, economics@westpac.com.au

Things you should know.

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