ACCI–Westpac Survey of Industrial Trends

Australian Chamber of Commerce and Industry & Westpac Banking Corporation

243rd report June 2022 (survey conducted from 12 May to 3 June)

- 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 survey finds that business conditions in the manufacturing sector expanded at a robust pace in the June quarter, with an increase in momentum associated with the reopening of the Australian economy.
- The Westpac-ACCI actual composite index lifted to 64.5 in the June quarter, with a reading above 50 indicating an expansion. That is up from 56.7 in March and from around 51 over the second half of 2021, during the delta lockdowns. This represents a return to conditions prevailing pre delta.
- Output and new orders expanded at a faster pace in the June quarter of 2022. Manufacturers responded to this by growing their workforce and increasing overtime - also both at a faster rate than in March.
- Manufacturing is benefitting from the rebound in activity with the reopening. Consumers are spending more freely with fewer covid related restrictions. Government spending is also trending higher, so too business investment, across equipment and infrastructure projects.
- Expectations are positive, with the Westpac-ACCI expected composite at 67.5, indicating respondents are anticipating that new orders and output will advance at a healthy clip in the September quarter.
- While the activity indicators are positive, the survey indicates that upside on growth is being capped by significant and persistent headwinds - notably labour and material shortages.
- Manufacturers' ability to produce is being hampered by labour constraints, which are the most acute since 1974, and difficulties in sourcing materials, which are the most pronounced since the oil shock of the mid-1970s. This reflects global supply bottlenecks and border closures.
- A net 51.7% of respondents indicated that labour was "harder to find" in the June quarter, a dramatic deterioration from 26.3% in March and 5.7% a year ago.
- These supply headwinds are leading to rapidly rising costs. Manufacturers profit margins are being squeezed as escalating costs outpace higher prices.
- Cost pressures intensified further in June, as gas and energy prices surged. Some 59% of respondents reported higher average unit costs, the highest reading since the high inflation days of 1985/86.
- The clear message from this survey is that consumers should brace for further sharp price increases.

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
Ryan Wells, Analyst, 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 243rd consecutive survey was closed on 3 June 2022.

A total of **188** 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 and September 2022.

Key survey results

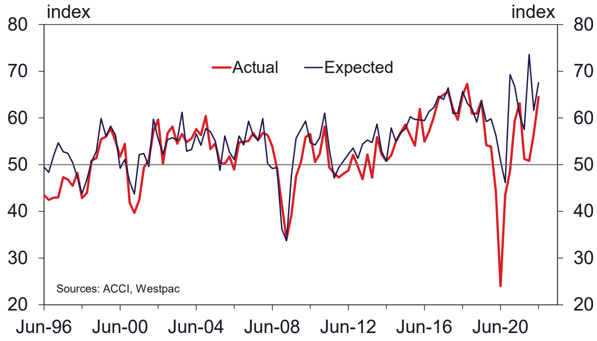
Westpac–ACCI Composites (seasonally adjusted)

	Q1 2022	Q2 2022
Actual – composite index	56.7	64.5
Expected – composite index	61.7	67.5

- The Westpac-ACCI Actual Composite continued to forge ahead in the June survey, rising to 64.5 from 56.7 in March.
- With a reading firmly above 50, this indicates that conditions are expanding at a robust pace. Increased momentum is evidence of strength in underlying demand, driving a further lift in orders and output.
- Despite working through omicron/weather related disruptions in Q1, supply-side issues, particularly around materials and labour inputs, are still present.
- At 67.5, the Expected Composite is at a very elevated level. This positive outlook reflects the expected strength in consumption through mid-year as the rebound in activity on reopening continues.

Westpac-ACCI Composite indexes

Actual & expected, sa

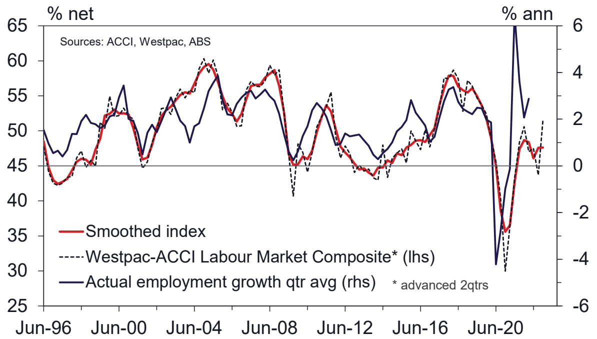


Westpac–ACCI Labour Market Composite

	Q1 2022	Q2 2022
Composite index	45.4	51.5

- The survey provides insights into economy-wide employment growth. This highlights the key linkages between manufacturing and the labour market.
- Over recent years, the Westpac-ACCI Labour Market Composite continued to broadly track the large swings in employment.
- In this update, the Labour Market Composite lifted to 51.5 from 45.4 in March. This is the highest print since the onset of the pandemic, eclipsing the 50.6 seen just prior to the delta outbreak in Q3.
- Official data confirms that employment conditions are healthy with annual employment growth at 2.9% for Q1 2022. With employment set to expand further, the unemployment rate will fall to even lower levels.

Labour Composite and employment trends



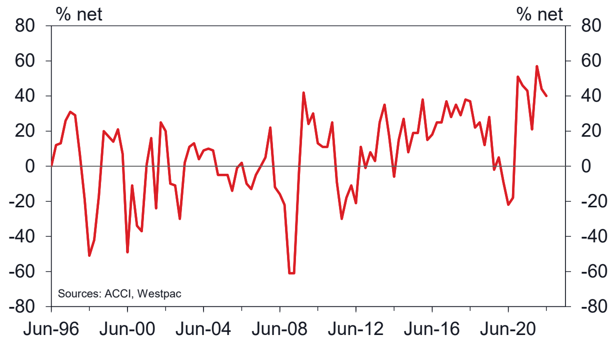
General business situation

	Q1 2022	Q2 2022
Net balance	44	40

- Manufacturing sentiment about the general business outlook proved to be buoyant in the March quarter despite omicron/weather disruptions.
- In the June quarter, respondents remained positive. A net 40% expect the general business situation to improve over the next six months. While down from a +57% in Q4, this is still well above average.
- This survey result is consistent with the general consensus that the Australian economy will likely continue to expand over this year, supported by pent-up consumer demand and a strong household balance sheet.
- However, with an RBA interest rate tightening cycle now underway, the risk is that storm clouds form on the horizon, with a potential slowdown into 2023.

General business situation

Next six months



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.

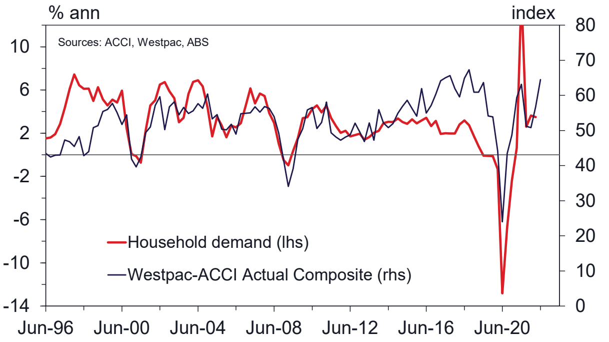
The business cycle & economic outlook

Manufacturing & the business cycle

- The Westpac-ACCI Actual Composite index has a solid track record of predicting near-term domestic economic conditions and identifying turning points in the cycle.
- Fluctuations in the stringency of health restrictions have been central to the consumer's ability to spend during the pandemic and in turn the fortunes of the manufacturing sector.
- The ongoing rebound in activity from the conclusion of lockdowns, and the passing of weather related disruptions earlier this year, is associated with improved economic conditions.
- The manufacturing sector gained momentum in the June quarter, likely mirroring a strengthening of conditions across the broader economy - led by consumers spending more freely.

Manufacturing and the business cycle

Westpac-ACCI Composite & household demand

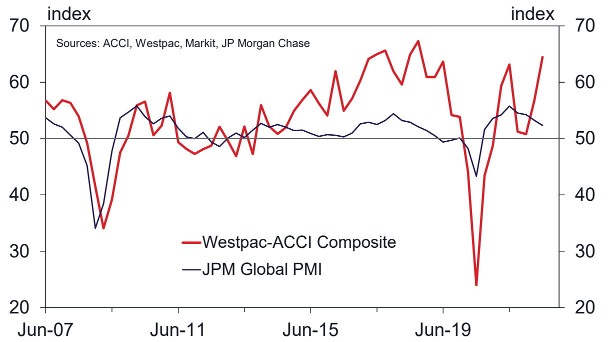


Australian & World manufacturing surveys

- Global and Australian manufacturing cycles tend to be synchronised, especially at major turning points. Historically, the Westpac-ACCI Actual Composite has moved broadly in line with global manufacturing conditions.
- Global manufacturing PMIs plummeted in April 2020 at the outset of the pandemic. Subsequently, the sector globally experienced a rapid recovery.
- In 2022, the manufacturing sector globally has - in aggregate - remained comfortably in the expansion zone, notwithstanding the challenges of COVID-19.
- The US and Eurozone manufacturing PMIs printed at healthy levels in May (56.1 and 54.6 respectively). China's Caixin manufacturing PMI has underperformed in 2022, moderating to 48, down from 51 at end-2021, reflecting a loss of momentum due to ongoing COVID disruptions.

Australian & World manufacturing surveys

Westpac-ACCI & Global PMI indexes

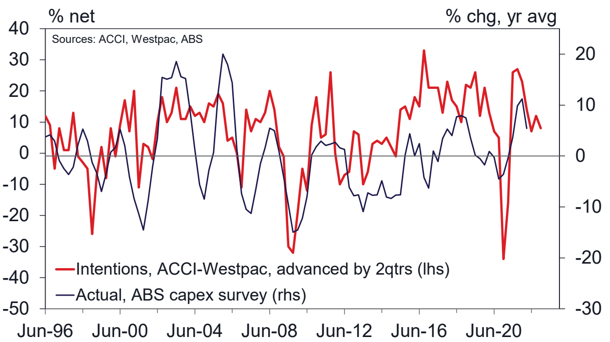


Manufacturing & business investment

- The ACCI-Westpac survey has a solid track record of predicting equipment investment by the manufacturing sector.
- The survey finds that while investment intentions are still positive, they have cooled of late.
- In June, a net 8% of respondents intend to increase equipment spending over the next 12 months. That is down from 12% in March and well off the highs seen from late 2020 and over the first half of 2021 - when Australia emerged from the initial lockdown.
- Official ABS data confirms this broad picture. The sector boosted spending on equipment late in 2020 and early 2021, with sizeable gains. Since then, the picture has been more mixed. Spending pulled-back with the onset of the delta lockdowns in 2021 Q2. A nascent recovery is evident late in 2021 and the opening quarter of 2022.

Manufacturing equipment investment

Intentions (survey) vs actuals (ABS data)



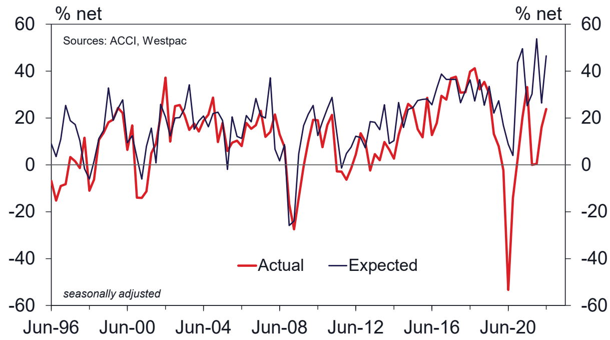
Activity & orders

Output (seasonally adjusted)

	Q1 2022	Q2 2022
Actual – net balance	16	24
Expected – net balance	26	46

- The survey indicates a lift in momentum, with manufacturing output expanding at a faster pace in the June quarter. A net 24% of respondents increased output in Q2, up from a net 16% in Q1.
- Fewer disruptions and the ongoing strength in household spending have been key areas of support for output growth.
- However, acute labour and material shortages are cited as a primary constraint to production, tempering the full potential of output expansion.
- Expectations have improved markedly over Q2. A net 46% of firms expect output will increase over the next three months, reflecting optimism around the expected strength of consumption over this year.

Output growth
Actual & expected

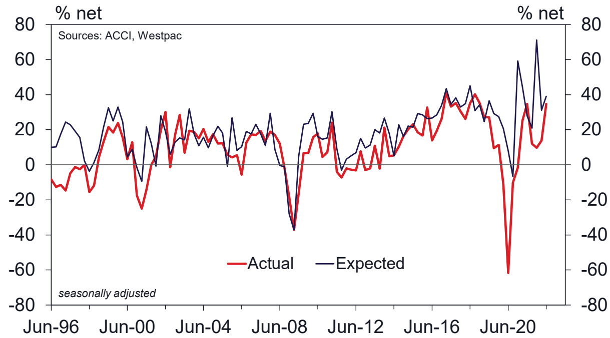


New orders (seasonally adjusted)

	Q1 2022	Q2 2022
Actual – net balance	14	35
Expected – net balance	31	39

- The expansion in new orders shifted into a higher gear in June, with a net 35% of respondents reporting rising new orders in the quarter. This compares to a net 14% in March, matching the level seen before the delta outbreak.
- The prospects for new orders have been buoyed by the strength of consumer spending as the recovery ensues. However, housing conditions remain mixed, with approvals well down from their highs and significant cost pressures eroding profitability.
- Consistent with firms' perceptions of the business outlook, a net 39% of respondents expect new orders will rise in the next three months.

New orders
Actual & expected

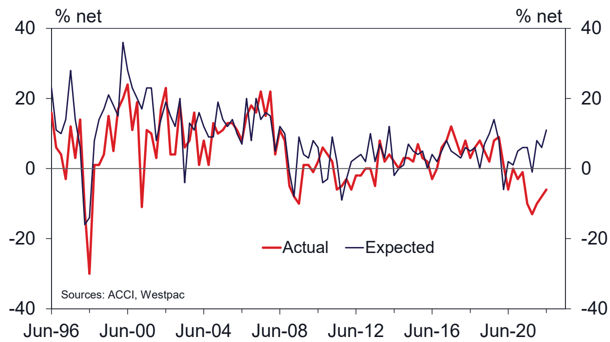


Exports

	Q1 2022	Q2 2022
Actual – net balance	-8	-6
Expected – net balance	6	11

- Export conditions remain challenging, the survey reports.
- Exports declined over the June quarter, with a net 6% of firms reporting a reduction. This marks yet another quarter of contraction, following a net 13%, 10% and 8% reduction in the previous three quarters.
- Supply headwinds, around freight and shipping costs, alongside patchiness in global export demand, most recently from Europe, are the key concerns of manufacturers.
- Expectations improved in Q2, with a net 11% of respondents anticipating an increase in exports over the next three months.

Export deliveries
Actual & expected



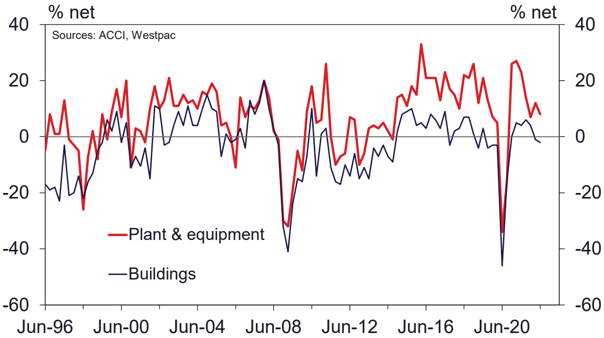
Investment & profitability

Investment intentions

	Q1 2022	Q2 2022
Plant & Equipment – net balance	12	8
Building – net balance	–1	–2

- Investment intentions declined slightly in the June survey, holding at a mildly positive but subdued level.
- Firms are still looking to invest but not to the same degree of confidence seen from late 2020 and over the first half of 2021 - when Australia emerged from the initial lockdown.
- A net 8% of firms are intending to increase plant and equipment investment over the next 12 months, moderating from a net 12% in the March quarter and well down from a net 27% early in 2021.
- Building projections for the year ahead remain broadly unchanged and soft, with a net 2% planning a decrease.

Investment intentions
Next twelve months

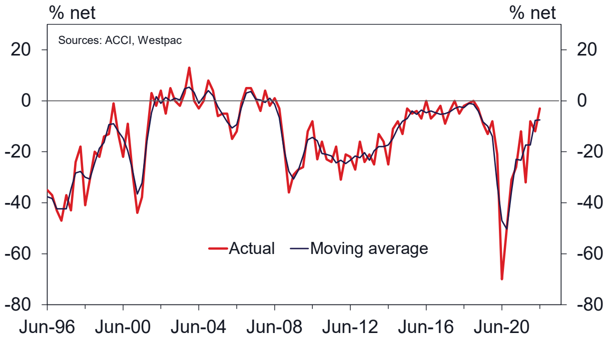


Capacity utilisation

	Q1 2022	Q2 2022
Net balance	–12	–3

- Disruptions throughout the March quarter acted as speed bumps to the early stages of the recovery this year. As a result, the proportion of firms reporting underutilisation moved from a net 8% in December to a net 12% in March.
- Move forward to June, and firms regained some of their momentum. A greater proportion of firms are operating above capacity (9% to 15%) and fewer firms are operating below capacity (21% to 18%).
- This contributed to the net number of firms operating below capacity improving from 12% to 3%
- Significant supply headwinds - including ongoing material and labour shortages - have impacted the ability of some firms to operate at capacity.

Capacity utilisation

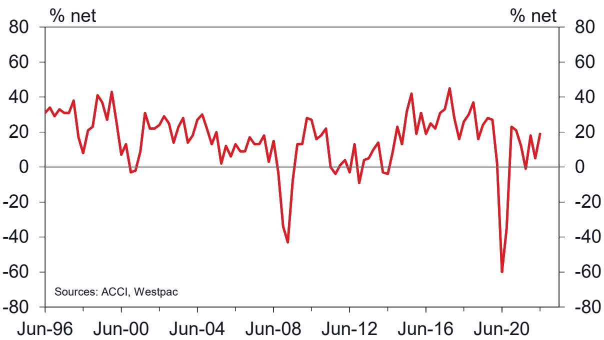


Profit expectations

	Q1 2022	Q2 2022
Net balance	5	19

- The profitability of the manufacturing sector took a hit in Q1 as cost pressures and supply headwinds continued to intensify.
- In the latest survey, profit expectations bounced off their lows, with a net 19% of respondents expecting profits will rise in the coming twelve months - broadly in line with the long-run average.
- The positive is that the ongoing rebound in activity will see a lift in turnover.
- However, the upside is capped by cost pressures and supply headwinds which are still weighing heavily on the manufacturing sector. Margins are being squeezed by these intense cost pressures.

Profit expectations
Next twelve months



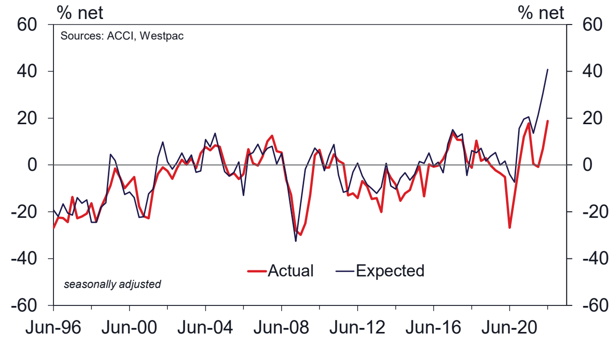
The labour market

Numbers employed (seasonally adjusted)

	Q1 2022	Q2 2022
Actual – net balance	7	19
Expected – net balance	31	41

- The June survey indicates that employment dynamics in the manufacturing sector improved materially in the period. A net 19% of firms increased employment in the quarter, up from a net 7% in Q1, a result constrained by the omicron outbreak.
- However, employment outcomes are visibly strained - with actual outcomes falling substantially short of expectations (plans) - evidence of acute labour shortages.
- Expectations for future employment remain highly positive, with a net 41% of firms intending to grow their workforce next quarter. Given recent experience and the prospect of a tighter labour market ahead, firms will be unlikely to meet these expectations.

Numbers employed
Actual & expected

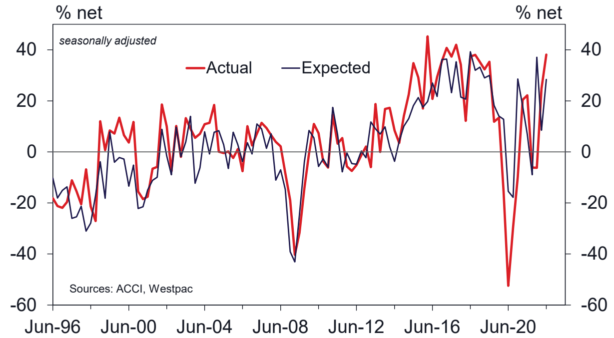


Overtime worked (seasonally adjusted)

	Q1 2022	Q2 2022
Actual – net balance	25	38
Expected – net balance	8	28

- The use of overtime saw a further and sizeable lift in the June quarter, with a net 38% of firms reporting an increase in overtime. This beat manufacturers own expectations, whereby only a net 8% anticipated a lift in overtime in June.
- At a time of rising output and constrained employment outcomes, manufacturers have turned to the use of additional overtime to fill the void.
- Overtime expectations lifted considerably in June, with a net 28% of respondents foreseeing an increase in overtime in the coming months. With the prospect of a burst in output through mid-year and ongoing labour shortages, the use of overtime will likely continue to be seen.

Overtime worked
Actual & expected

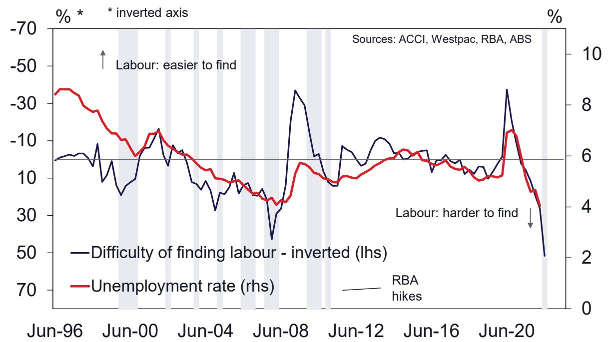


Difficulty of finding labour (seasonally adjusted)

	Q1 2022	Q2 2022
Net balance	26.3	51.7

- 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.
- Since early last year, manufacturers have reported increasingly challenging conditions for finding labour. This issue intensified drastically in Q2, with a net 51.7% of respondents indicating that labour was "harder to find". These are the tightest conditions in the history of this series, dating back to 1974, and compares with an end 2007 reading of 42.8.
- A critical undersupply of labour during a time of strong demand has the unemployment rate below 4% for the first time since 1974. With the labour market set to tighten further, firms will likely continue to find difficulty in sourcing labour.

Labour market tightness



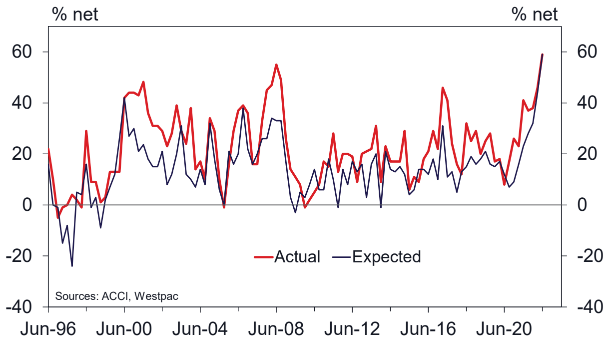
Prices & inflation

Average unit costs

	Q1 2022	Q2 2022
Actual – net balance	46	59
Expected – net balance	44	59

- In the June quarter, input cost pressures became even more acute, with a net 59% of manufacturers reporting higher input costs. That is the highest reading since the 1985/86 period.
- Both "labour" and "materials" continue to be cited as constraints to output expansion at historically elevated levels - dynamics that are eroding profitability in the sector through rising costs. Surging gas and energy costs are compounding the challenges faced by the sector.
- Manufacturers expect that intense cost pressures will persist, with a net 59% reporting they anticipate average costs will rise further in the period ahead. This is up from a net 44% in the March survey.

Average unit costs
Actual & expected

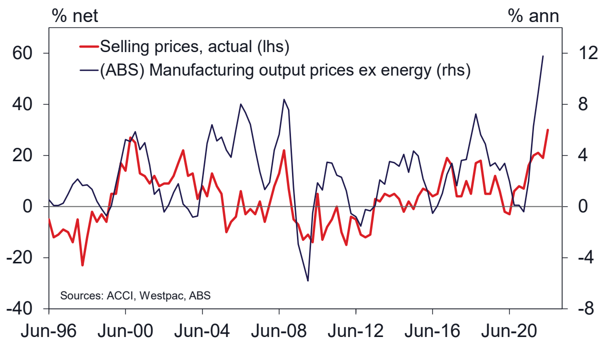


Average selling prices

	Q1 2022	Q2 2022
Actual – net balance	19	30
Expected – net balance	26	36

- Margins are being squeezed with only a partial pass through of higher costs to consumers. Selling price increases continue to trail the rise in average costs.
- This dynamic was again evident in the June quarter and will likely continue. The proportion of firms reporting an increase in selling prices was 30% in the period (up from 19% last quarter). That is substantially below the net 59% reporting a rise in average unit costs over the same period.
- Consumers should brace for further sharp rises in prices the survey suggests, as costs spiral. A net 36% of respondents expect selling prices will rise over the next three months.

Manufacturing upstream price pressures

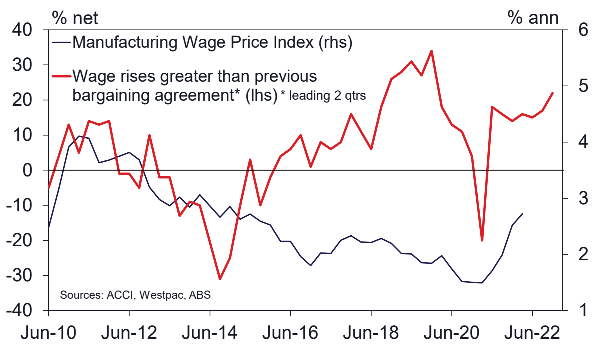


Manufacturing wages

	Q1 2022	Q2 2022
Net balance	17	22

- Wage pressures are building as the labour market tightens further. The survey reports that firms expect further upward pressure in future enterprise bargaining agreements, a turnaround from the decline observed at the outset of the pandemic.
- In the June quarter, a net 22% of respondents anticipate that their next enterprise wage agreement will deliver an outcome above their last. That is an increase from the net 15% and 17% in Q4 and Q1.
- The recent lift in manufacturing wage expectations is consistent with the direction of official data. The ABS reports an acceleration of manufacturing wages growth, with the six-month annualised pace climbing to in excess of 3%, well above that pre-pandemic.

Manufacturing wage growth



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Factors limiting production

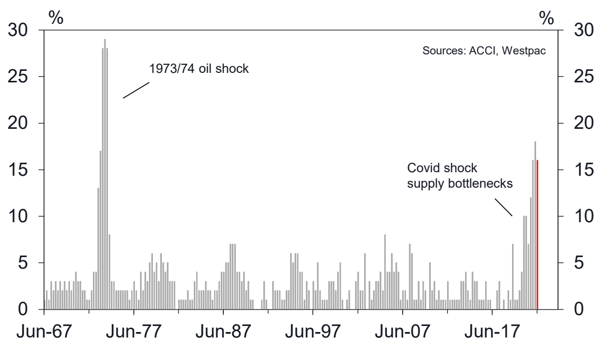
Factors limiting production

- The latest survey confirms that the manufacturing sector is facing ongoing significant supply headwinds.
- "Material" constraints have been a factor over the past year, remaining at a historically elevated level in the June quarter - comparable to the 1974 oil shock, as bottlenecks emerge, locally and globally.
- Strong demand and an undersupply of labour have led 25% of manufacturers to cite labour as the single factor most limiting production - the highest since 1974 (when unemployment was last below 4%) and well above the 2007 pre-GFC high of 16%.
- The proportion of firms who identified "other" factors as most limiting moderated to 14% from 19%, as COVID-19 related disruptions continued to fade.
- Respondents citing orders as the single factor most limiting production was broadly unchanged, at 41%, well below the long run average of 64%.

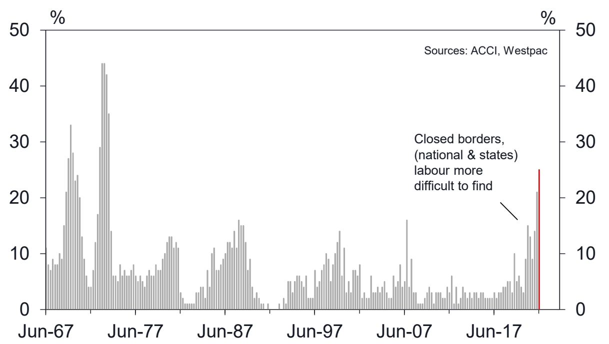
Factors limiting production

	Q4 2021	Q1 2022	Q2 2022
Orders (%)	39	39	41
Capacity (%)	2	2	2
Labour (%)	14	21	25
Finance (%)	2	0	2
Materials (%)	16	18	16
Other (%)	26	19	14
None (%)	1	1	0

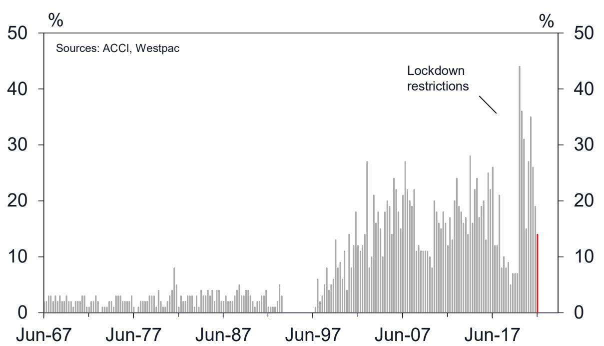
Materials: "single factor" most limiting production



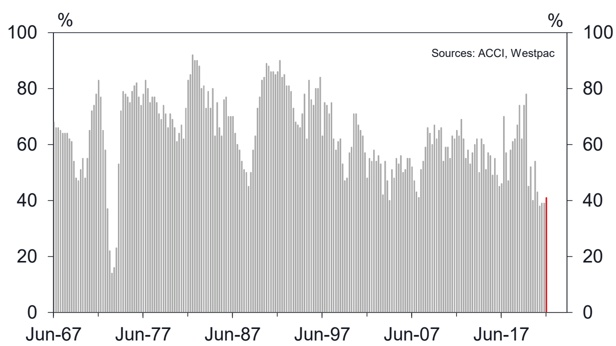
Labour: "single factor" most limiting production



"Other": single factor most limiting production



Orders: "single factor" most limiting production



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
40	53	34	13

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

Net balance	Above Normal	Normal	Below Normal
-3	15	67	18

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

None	0	Orders	41
Material	16	Finance	2
Labour	25	Capacity	2
Other	14		

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?	45	47	51	2
(b)	finance?	-1	4	91	5

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

		Net balance	Greater	Same	Less
(a)	on buildings?	-2	10	78	12
(b)	on plant & machinery?	8	24	60	16

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	19	75	6	39	41	57	2
7.	Overtime worked	30	34	62	4	25	37	51	12
8.	All new orders received	26	38	50	12	39	46	47	7
9.	Orders accepted but not yet delivered	24	28	68	4	6	18	70	12
10.	Output	19	39	41	20	45	52	41	7
11.	Average costs per unit of output	59	60	39	1	59	60	39	1
12.	Average selling prices	30	30	70	0	36	36	64	0
13.	Export deliveries	-6	4	86	10	11	14	83	3
14.	Stock of raw materials	9	20	69	11	-2	13	72	15
15.	Stocks of finished goods	3	15	73	12	-1	9	81	10

Summary of results (not seasonally adjusted)

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

(a) Improve?	29
(b) Remain unchanged?	61
(c) Decline?	10
Net balance	**19**

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?	22
(b) Same?	78
(c) Less?	0
Net balance	**22**

A. Industry profile of survey:

	(% of respondents)
Food, beverages, tobacco	15
Textiles, fabrics, floor coverings, felt, canvas, rope	4
Clothing, footwear	5
Wood, wood products, furniture	2
Paper, paper products, printing	7
Chemicals, paints, pharmaceuticals, soaps, cosmetics petroleum & coal products	9
Non-metallic mineral products: glass, pottery, cement bricks	7
Basic metal products: processing, smelting, refining, pipes & tubes	6
Fabricated metal products: structural & sheet metal, coating & finishing, wire, springs, hand tools	13
Transport equipment: motor vehicles & parts, excluding repairs, rail, ships, aircraft, including repairs	5
Other machinery & equipment: electrical, industrial scientific, photographic	21
Miscellaneous: including manufacturers of leather, plastic & rubber, sporting equipment, jewellery	6

B. How many employees are covered by this return?

1-100	101-200	201-1000	Over 1000
50	12	18	20

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

WA	SA	VIC	NSW/ACT	QLD	TAS
12	9	25	34	15	5

The Westpac-ACCI Composite Indices

The Westpac-ACCI 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-ACCI 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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Publication enquiries, Economics, economics@westpac.com.au

Things you should know.

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