

ACCI–Westpac Survey of Industrial Trends

Australian Chamber of Commerce and Industry & Westpac Banking Corporation

181st report December quarter 2006

- The Westpac–ACCI Actual Composite index softened slightly in the December quarter from 56.2 to 54.9. It remains comfortably above its decade average, which is consistent with above–trend growth.
- This Survey captures manufacturers' assessments following the 0.25% interest rate increase on November 8.
- General business sentiment deteriorated slightly, which is likely to reflect softer expectations in the wake of the November rate hike, and ongoing pressure on profit margins.
- The Westpac–ACCI Expected Composite index fell from 57.6 to 53.8, which remains above the decade average and points to continuing above–trend growth, despite three recent interest rate hikes.
- Labour demand eased slightly, but the Labour Market Composite index remains consistent with solid jobs growth in 2007H1.
- Labour market conditions look to have tightened, with the 'difficulty of finding labour' index rebounding to recent highs.
- Despite the tight labour market, manufacturing enterprise bargaining wage expectations remain historically low.
- Selling prices fell slightly, contrary to strong expectations, and March quarter expectations have been pared back.
- Cost increases remain strong, but are expected to slow, presumably reflecting falling fuel prices.
- Capacity utilisation rose significantly to the third highest level in 17 years.
- Investment plans moderated to near historical averages, while the composite index is consistent with investment growth.
- Export deliveries rose further and are now well above the decade average, despite the strength in the Australian dollar.



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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 181st consecutive survey was conducted in the week ending 1 December 2006. A total of 252 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 in March 2007.

Past performance is not a reliable indicator of future performance. The forecasts given in this document 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 ultimate outcomes may differ substantially from these forecasts. Westpac Institutional Bank is a division of Westpac Banking Corporation ABN 33 007 457 141. Information current as at date above. This information has been prepared without taking account of your objectives, financial situation or needs. Because of this you should, before acting on this information, consider its appropriateness, having regard to your objectives, financial situation or needs. Westpac's financial services guide can be obtained by calling 132 032, visiting www.westpac.com.au or visiting any Westpac Branch. The information may contain material provided directly by third parties, and while such material is published with permission, Westpac accepts no responsibility for the accuracy or completeness of any such material. Except where contrary to law, Westpac intends by this notice to exclude liability for the information. The information is subject to change without notice and Westpac is under no obligation to update the information or correct any inaccuracy which may become apparent at a later date. Westpac Banking Corporation is regulated for the conduct of investment business in the United Kingdom by the Financial Services Authority. If you wish to be removed from our e-mail, fax or mailing list please send an e-mail to economics@westpac.com.au or fax us on +61 2 8254 6934 or write to Westpac Economics at Level 2, 275 Kent Street, Sydney NSW 2000. Please state your full name, telephone/fax number and company details on all correspondence. © 2004 Westpac Banking Corporation.

Key survey results

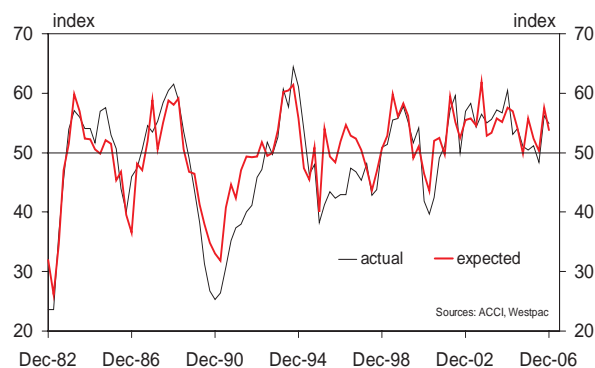
Westpac-ACCI composites, seasonally adjusted

	Q3 2006	Q4 2006
Actual – composite index	56.2	54.9
Expected – composite index	57.6	53.8

- The Actual Composite index edged back in the December quarter, falling 1.3pts to 54.9 after a 7.8pt surge previously. This was the second highest since 2004Q4.
- With the index comfortably above its decade average (51.8), it suggests activity growth has continued at an above-trend pace. The dip in the Actual Composite was driven by smaller than usual seasonal gains in all five components, with the strongest improvement in orders.
- The Expected Composite index fell 3.8pts to 53.8 after a 7.3pt jump previously, but remains above its decade average (53.2). The dip was due to a greater than usual seasonal drop in all expectations, particularly new orders.

Westpac-ACCI composite indexes

Actual & expected, sa

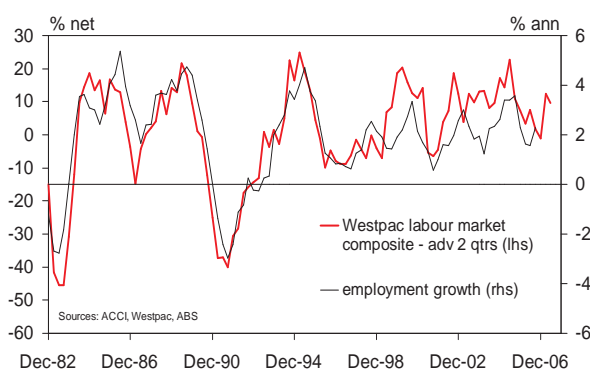


Westpac-ACCI labour market composite

	Q3 2006	Q4 2006
Net balance	12	10

- Manufacturing labour demand eased marginally in the quarter with the net balance of the Labour Market Composite index easing 2pts to 10, the second highest since 2005Q1 and still above its decade average of 7.
- The index has provided a reliable guide to future employment growth and remains consistent with a firmer annual pace through 2007H1. The dip in the index was driven by expected overtime, expected and actual employment, partially offset by stronger actual overtime.

Jobs growth to firm in H1 2007



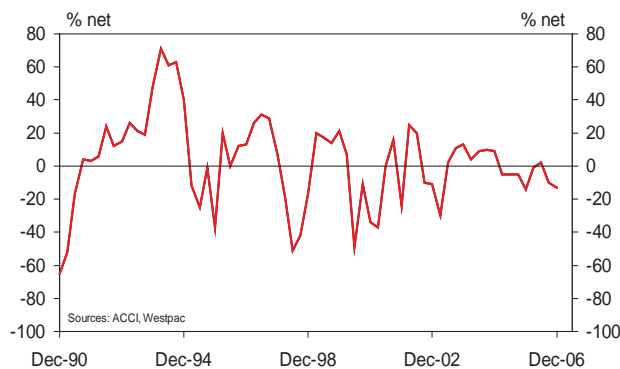
General business situation

	Q3 2006	Q4 2006
Net balance	-10	-13

- There was a further weakening, on balance, in business expectations in the December quarter 2006. The proportion of respondents expecting an improvement in the general business situation in the next six months was lower (14% vs 19%). The proportion predicting a deterioration was marginally lower (27% vs 29%), resulting in a net balance of -13% (vs -10% in the previous quarter). Well over half the respondents (59% vs 52%) expected no change.

General business situation

Next six months



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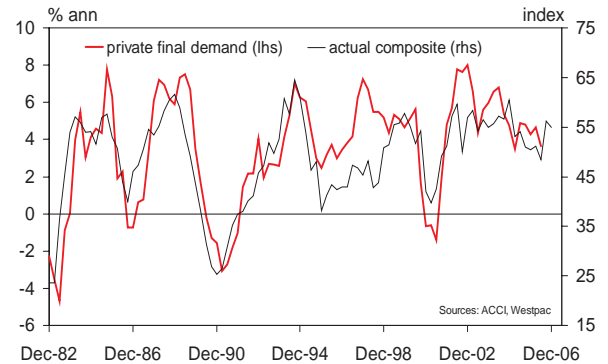
The business cycle & economic outlook

Westpac-ACCI survey & the business cycle

- The Westpac-ACCI Actual Composite index has a solid track record of predicting near-term economic growth, including picking turning points in the economic cycle.
- The minor dip in the composite index in the December quarter suggests firmer private final demand growth in 2006H2 after a relatively softer June quarter.
- At a level of 54.9 (vs 56.2 previously), the Actual Composite index remains consistent with above-trend growth in the December quarter, comfortably above its decade average of 51.8.

Manufacturing & the business cycle

Westpac-ACCI composite index & private demand

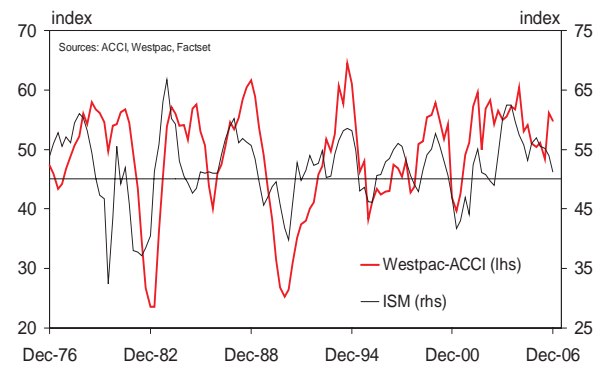


Australian & US manufacturing surveys

- The US and Australian manufacturing cycles have an historical tendency to move broadly in synch. However, through 2006H2 a divergent performance has been apparent, with Australian conditions improving at a time of deteriorating US conditions.
- The US manufacturing ISM survey readings have softened through 2006. The ISM index fell from a 2006Q2 average of 55.2 to 54.0 in Q3, easing further in early Q4 to 51.2 in October (lowest since 2003Q2). This slowing is no doubt a reflection of a significant weakening in the US housing sector over the last year.

Australian & US manufacturing surveys

Westpac-ACCI & ISM composite indexes

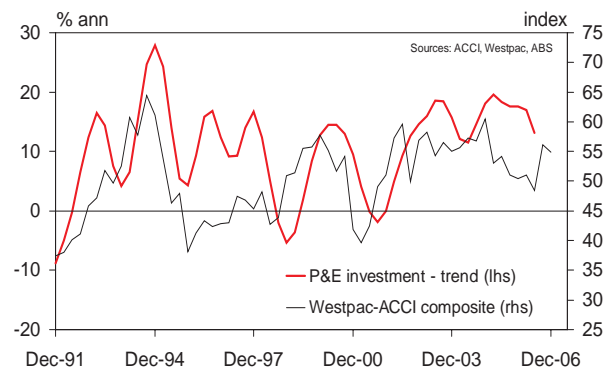


Westpac-ACCI survey & business investment

- The Actual Composite index also has a leading relationship with business investment spending, particularly on plant and equipment, although the link has weakened in recent years with the resources boom.
- The slight dip in the index implies a marginal softening in the manufacturing investment outlook, but total investment will remain supported by the mining sector.
- The level of the index remains comfortably in the territory associated with growing plant and equipment investment. The backdrop of healthy corporate balance sheets, firm global demand and tight capacity, also remains supportive of rising investment.

Activity & capital investment

Westpac-ACCI composite & plant & equipment investment



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Activity & orders

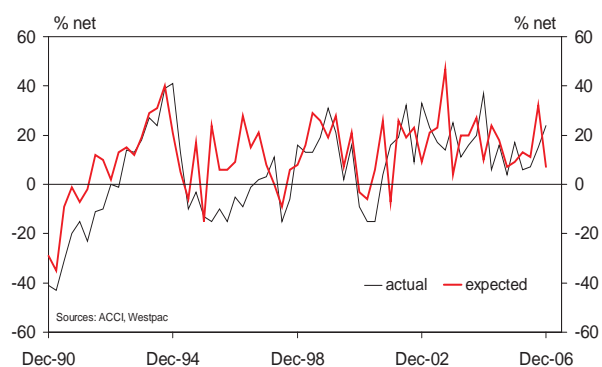
Output

	Q3 2006	Q4 2006
Actual – net balance	15	24
Expected – net balance	32	7

- While well short predictions of three months ago, the net output indicator continued to strengthen in the December quarter 2006. The proportion of respondents reporting a rise was higher (40% vs 31%) while those recording a decline remained unchanged at 16%, resulting in a net balance of 24% (vs 15%). Expectations for next quarter remain positive but much more modest than three months ago (7% vs 32%) and close to June quarter 2006 levels.

Output growth

Actual & expected



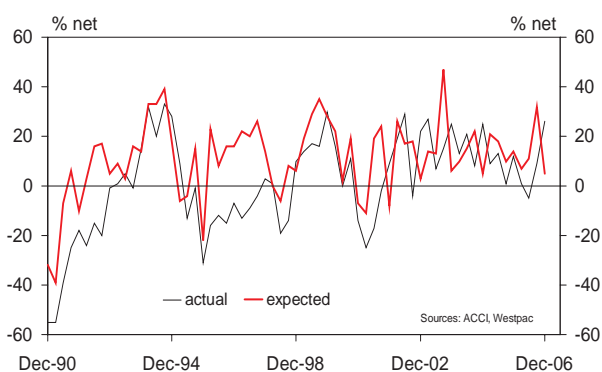
New orders

	Q3 2006	Q4 2006
Actual – net balance	9	26
Expected – net balance	32	5

- A similar trend was reflected by actual and predicted outcomes for new orders. The proportion of respondents reporting an increase in new orders rose strongly from 27% to 41%. The proportion reporting a decline eased (15% vs 18%), resulting in a robust net balance of 26% (vs 9%). Net forward projections for the next three months declined sharply (5% vs 32%).
- Reflecting the much stronger outcomes for new orders, the net indicator for orders accepted but not yet delivered also strengthened in the December quarter 2006 (13% vs -5%). However, predictions for the March quarter 2007 have been sharply downgraded and turned negative (-16% vs 7%).

New orders

Actual & expected



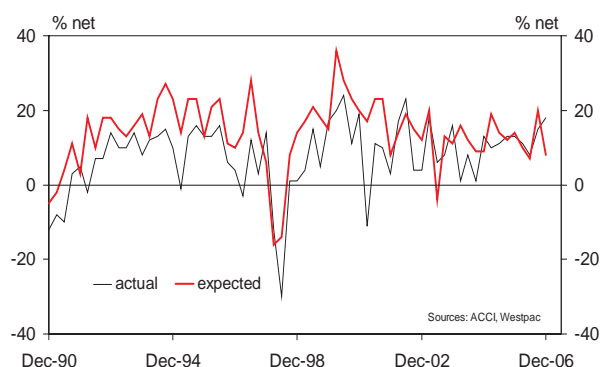
Exports

	Q3 2006	Q4 2006
Actual – net balance	15	18
Expected – net balance	20	8

- Export deliveries improved, albeit modestly, in the December quarter 2006. The proportion of respondents reporting a rise in export deliveries rose (21% vs 18%). Those recording a decline remained unchanged at 3%, resulting in a net outcome of 18% (vs 15%). However, while remaining positive, predictions for the next three months have declined sharply (8% vs 20%), likely a reflection of the higher Australian dollar.

Export deliveries

Actual & expected



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Investment & profitability

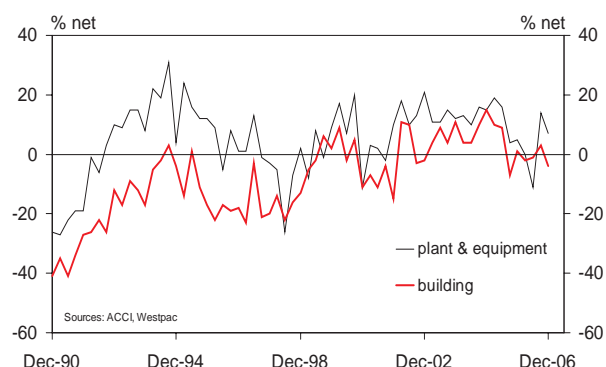
Investment intentions

	Q3 2006	Q4 2006
Plant & Equipment – net balance	14	7
Building – net balance	3	-4

- While still firm, manufacturers' plans for plant and equipment investment spending in the next 12 months were well below the very robust levels of three months ago. Of the manufacturers surveyed, 23% (vs 30%) reported plans to increase their spending. The proportion expecting a decline was unchanged (16%), resulting in a net balance of 7% (vs 14%). A higher proportion (61% vs 54%) expected no change.
- Spending plans for buildings also softened, with 13% (vs 18%) of the respondents predicting an increase and 17% (vs 15%) a decline, resulting in a net outcome of -4% (vs 3%). The outcome is on par with its decade average (-2%), but above its full history average (-11%).

Investment intentions

Next twelve months

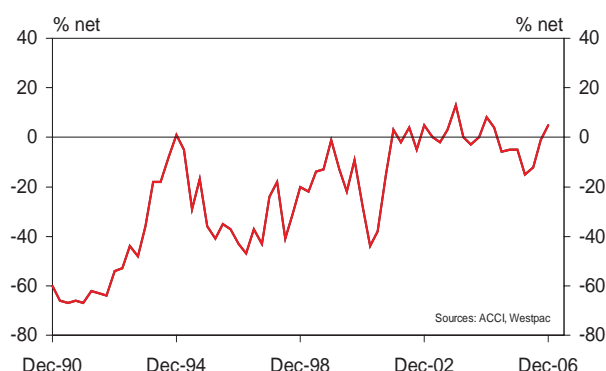


Capacity utilisation

	Q3 2006	Q4 2006
Net balance	-1	5

- The reported level of capacity utilisation increased again in the December quarter 2006. Almost one quarter of respondents reported working above their normal capacity (24% vs 18%). Those working below their normal capacity remained unchanged (19%), resulting in a net balance of 5% (vs -1%). This is the highest since 2004Q4 and the third highest since 1989Q2. Well over half the respondents (57% vs 63%) reported working at normal capacity levels.

Capacity utilisation



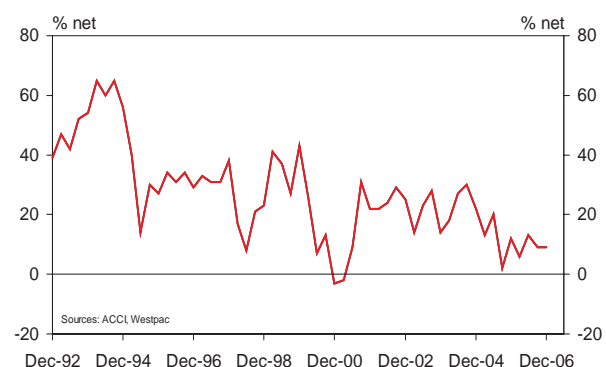
Profit expectations

	Q3 2006	Q4 2006
Net balance	9	9

- Profit expectations were virtually unchanged in the December quarter 2006. The proportion expecting higher profits in the next 12 months eased further (27% vs 32%), but those predicting a decline was also lower (18% vs 23%), resulting in an unchanged net balance of 9%. This remains well below the decade average (20) despite strong actual output and orders, likely reflecting softer activity expectations and continued pressure on margins.

Profit expectations

Next twelve months



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The labour market

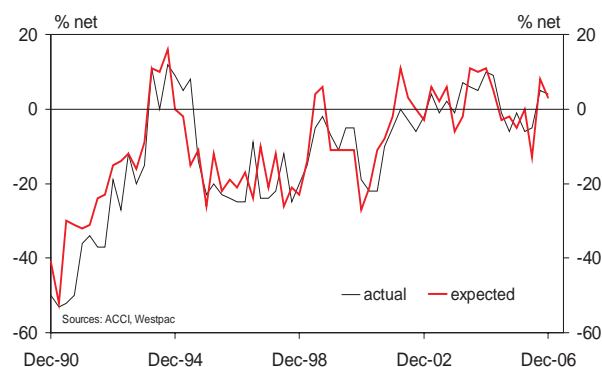
Numbers employed

	Q3 2006	Q4 2006
Actual – net balance	5	4
Expected – net balance	8	3

- The labour market remained virtually unchanged in the December quarter 2006. The proportion of respondents recording an increase in numbers employed rose marginally (19% vs 18%). Those reporting a decrease also edged up (15% vs 13%), resulting in a net balance of 4% (vs 5%). The net outlook for the next three months softened (3% vs 8%), but remains positive and well above its decade average (–6%).

Numbers employed

Actual & expected



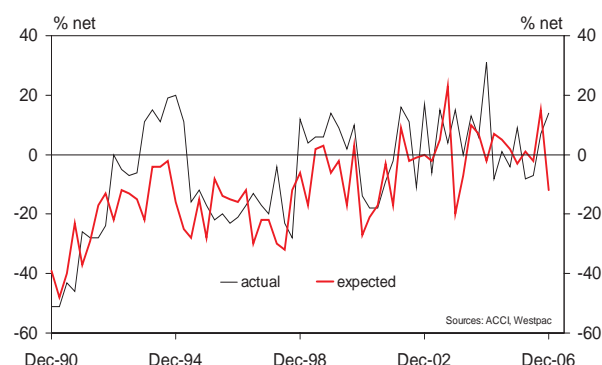
Overtime worked

	Q3 2006	Q4 2006
Actual – net balance	7	14
Expected – net balance	15	–12

- In line with predictions, the net overtime worked indicator doubled from 7% to 14%. A third of the respondents (32% vs 25%) reported higher levels of overtime worked while the proportion reporting a decline remained unchanged at 18%. Half the respondents (50% vs 57%) reported no change. However, a slump in overtime worked is predicted for the next three months (–12% vs 15%).

Overtime worked

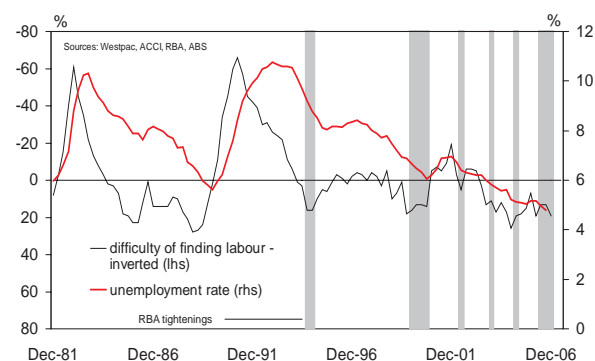
Actual & expected



Labour market tightness

- Despite the slight softening in labour demand indicators in the December quarter survey, respondents reported an increase in the difficulty of finding appropriately skilled labour. The net balance reporting labour as 'harder to get' rose to 19% from 13% previously, well above the decade average (6%) and within sight of the 2004Q4 peak of 26%.
- This historically high level of labour market tightness, combined with the resilience in the Labour Market Composite index, suggests the unemployment rate can remain around its 30 year low of 4.6%.

Difficulty of finding labour



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Prices & inflation

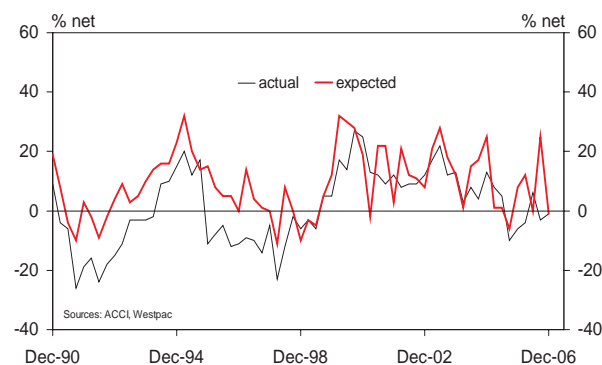
Average selling prices

	Q3 2006	Q4 2006
Actual – net balance	-3	-1
Expected – net balance	25	-1

- Contrary to predictions, there was little change in average selling prices in the December quarter 2006. Instead of rising sharply, the net prices indicator remained soft and marginally negative. The proportion of respondents reporting price increases was higher (21% vs 13%) but those recording a decline also rose (22% vs 16%), resulting in net balance of -1% (vs -3%), with 57% (vs 71% previously) reporting no change. A similar net outcome is predicted for the March quarter 2007 (-1% vs 25%) with 59% (vs 61%) expecting no change.

Average selling prices

Actual & expected



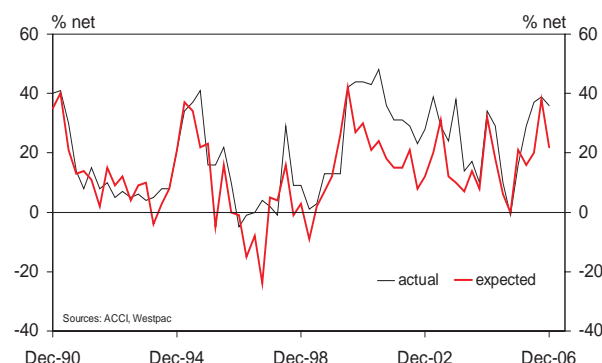
Average unit costs

	Q3 2006	Q4 2006
Actual – net balance	39	36
Expected – net balance	38	22

- On balance, the actual net outcome for average unit costs remained historically high in the December quarter at 36% (vs 39%). The proportion of manufacturers surveyed reporting rising costs eased slightly (43% vs 46%). Those recording decreases remained unchanged (7%). On balance, the pace of cost increases is expected to slow down in the next three months (22% vs 38%), but remains above the decade average (13%) and well in excess of expected selling prices, implying ongoing margin pressures.

Average unit costs

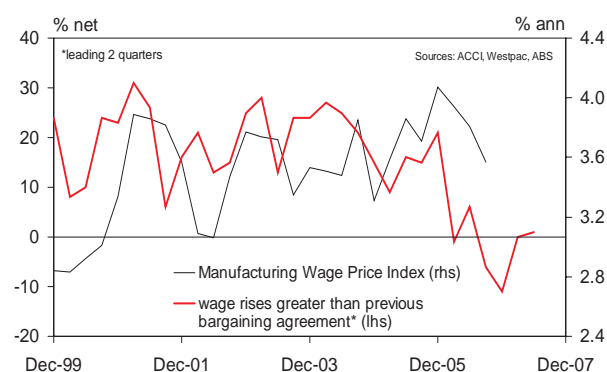
Actual & expected



Manufacturing wages

- Despite the increased difficulty of finding labour and resilient labour demand indicators, manufacturing wage expectations increased minimally in the quarter.
- 19% of respondents expect wage rises in their firm's next round of enterprise agreements to be higher than the previous agreement outcome, and 18% lower, giving a 1% net balance (vs 0% previously). This remains well below the decade average (12%) and implies a further easing in manufacturing wage growth into 2007, which has already eased (using manufacturing wage price index) from a 2005Q4 peak of 4.1%yr to 3.6%yr in 2006Q3.

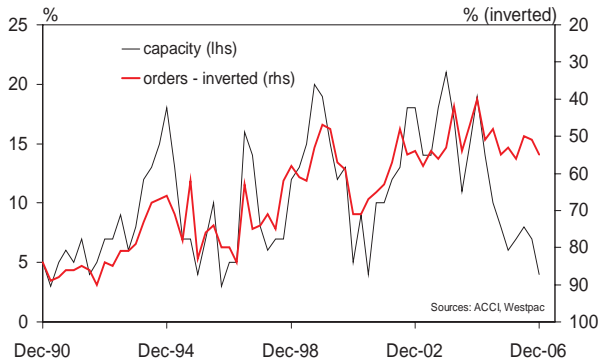
Manufacturing wages to decelerate further



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Other results

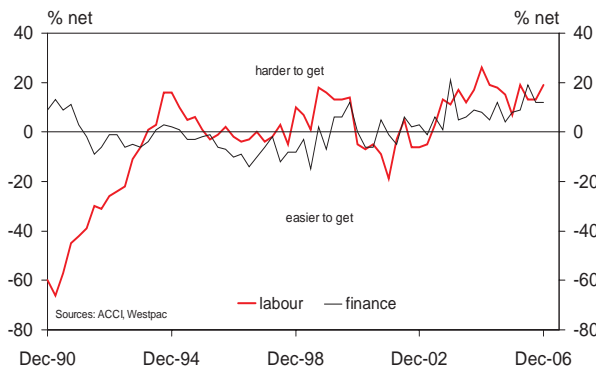
Key factor limiting production
% of respondents



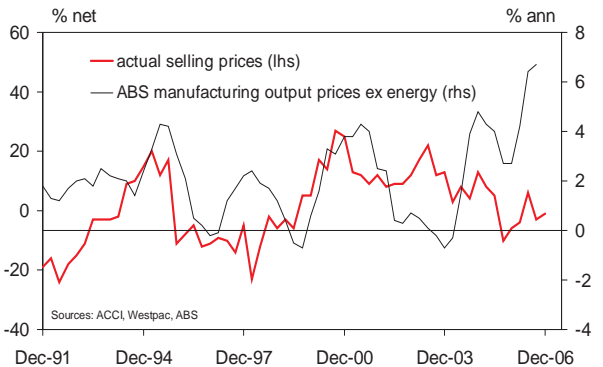
Factors limiting production

	Q2 2006	Q3 2006	Q4 2006
Orders (%)	50	51	55
Capacity (%)	8	7	4
Labour (%)	4	5	8
Finance (%)	4	3	1
Materials (%)	4	5	4
None (%)	6	7	10
Other (%)	24	22	18

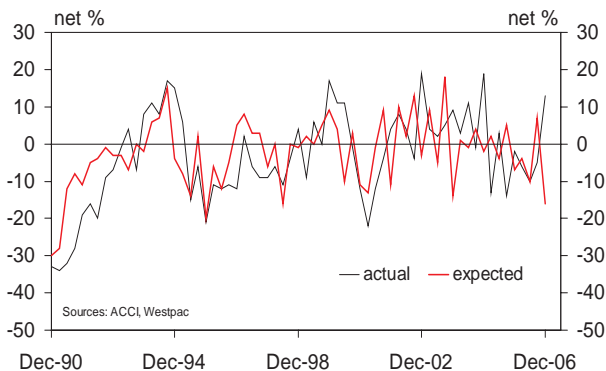
Availability of labour & finance



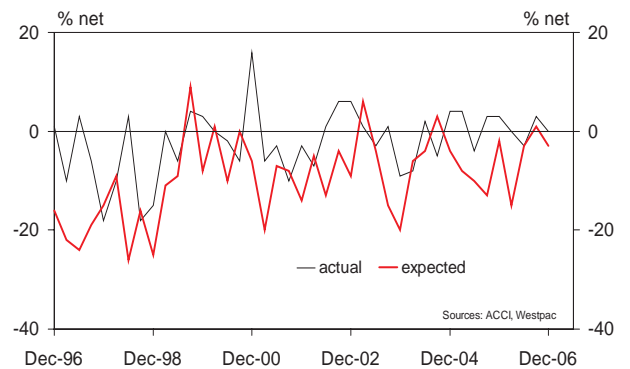
Mfg upstream price pressures should ease



New orders accepted but not delivered
Actual & expected



Stocks of finished goods
Actual & expected



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Summary of results

1. Do you consider that the general business situation in Australia will improve?

Net balance	Improve	Same	Deteriorate
-13%	14%	59%	27%

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

Net balance	Above normal	Normal	Below normal
+5%	24%	57%	19%

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

Orders	55%	Finance	1%
Capacity	4%	Labour	8%
Materials	4%	None	10%
Other	18%		

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?	+19%	23%	73%	4%
(b) finance?	+12%	20%	72%	8%

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

	Net balance	Greater	Same	Less
(a) on buildings?	-4%	13%	70%	17%
(b) on plant & machinery?	+7%	23%	61%	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:

	<i>Change in position in the last 3 months</i>			<i>Expected change during the next 3 months</i>				
	Net balance	Up	Same	Down	Net balance	Up	Same	Down
6. Numbers employed	+4%	19%	66%	15%	+3%	14%	75%	11%
7. Overtime worked	+14%	32%	50%	18%	-12%	15%	58%	27%
8. All new orders received	+26%	41%	44%	15%	+5%	26%	53%	21%
9. Orders accepted but not yet delivered	+13%	28%	57%	15%	-16%	13%	58%	29%
10. Output	+24%	40%	44%	16%	+7%	26%	55%	19%
11. Average costs per unit of output	+36%	43%	50%	7%	+22%	29%	64%	7%
12. Average selling prices	-1%	21%	57%	22%	-1%	20%	59%	21%
13. Export deliveries	+18%	21%	76%	3%	+8%	12%	84%	4%
14. Stock of raw materials	-6%	6%	82%	12%	-4%	8%	80%	12%
15. Stocks of finished goods	0%	10%	80%	10%	-3%	9%	79%	12%

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Summary of results

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

(a) Improve?	27%
(b) Remain unchanged?	55%
(c) Decline?	18%
Net balance	+9%

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?	19%
(b) Same?	63%
(c) Less?	18%
Net balance	+1%

A. Industry profile of survey:

	(% of respondents)
Food, beverages, tobacco	11
Textiles, fabrics, floor coverings, felt, canvas, rope	1
Clothing, footwear	4
Wood, wood products, furniture	5
Paper, paper products, printing	12
Chemicals, paints, pharmaceuticals, soaps, cosmetics petroleum & coal products	6
Non-metallic mineral products: glass, pottery, cement bricks	10
Basic metal products: processing, smelting, refining, pipes & tubes	2
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	14

B. How many employees are covered by this return?

1-100	101-200	201-1000	Over 1000
46%	17%	17%	20%

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

WA	SA	VIC	NSW	QLD	TAS
6%	11%	24%	38%	16%	5%

The Westpac-ACCI Composite Indices

The Westpac-ACCI actual and expected composite indices are weighted averages of the various 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 labour demand indicator is a weighted average of current and expected labour indicators from the Westpac-ACCI survey. The indicator is expressed as a detrended net balance. Approximate weights are as follows: employment 40%; expected employment 20%; overtime 30%; and expected overtime 10%.

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