

Business Prospects for Australian Manufacturing in 2008



Moderate year forecast amid belt tightening ...



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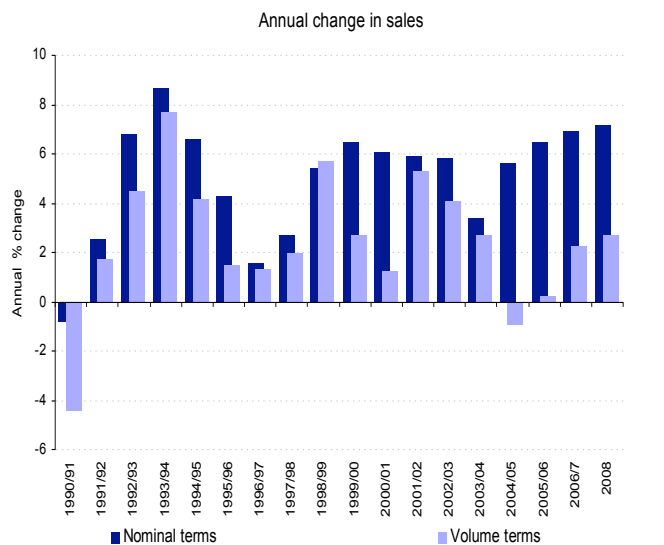
Moderate year forecast amid belt tightening ...

Summary

- Australian manufacturers are anticipating moderate growth in 2008, against a background of belt tightening as the sector faces continuing global uncertainty and potential softening in demand. While nominal sales are expected to repeat the strong performance of 2006/7, growth in volume terms will remain moderate.
- Nominal sales are expected to rise by 7.2% in 2008 (marginally higher than the 6.9% rise in 2006/7). However, adjusting for goods price movements, sales volumes are expected to increase by a modest 2.7% (just above the medium term average).
- The sales performance will be driven in large part by domestic demand, as the continuation of a strong Australian dollar weakens export performance.
- Nominal export growth is expected to be 7.5% in 2008, well down on the growth of 13.7% in 2006/7. Price movements, particularly for metals and fuel, however have inflated nominal export performance in recent years. Adjusting for these movements, suggests in volume terms, manufacturing exports will grow by 0.5% in 2008, down from 3.4% in 2006/7.
- As a precaution against potential softening in demand conditions, manufacturers are tightening their belts, with growth in capital expenditure and research and development expected to slow, and companies making greater use of imported goods and production inputs.
- Expenditure on new capital equipment is expected to fall for a second consecutive year, dropping by 1.2%, while expenditure on research and development is forecast to rise by less than 1%, after an estimated 4.2% rise in 2006/7. Use of offshore materials (as a percentage of sales) is estimated to rise to 32% from 31.7%
- Manufacturers are expected to make greater use of new products to improve competitiveness in 2008, the ratio of new products to sales rising from 21.2% in 2007 to 23.1%.
- Offsetting these savings, will be an increase in manufacturing employment of 2.2% (for the second consecutive year), as manufacturers continue to lift production to meet rising demand.
- Selling prices are expected to creep marginally higher, to 4.5%, with average wages expected to rise by 4.6%.
- The survey was conducted in late December 2007, covering over 500 manufacturers across all states. It precedes the recent reversal in financial markets since January 2008.

Sales

- Nominal sales (based on ABS data) rose by 6.9% in 2006/7. However, after taking into account price increase, the sector experienced an overall 2.2% rise in sales volumes, a significant improvement on the previous two years.
- Prospects for 2008 appear set to remain steady, although in volume terms the sector is forecasting only a moderate lift in sales.
- Nominal sales are forecast to rise by 7.2%, but in volume terms, forecast to grow by 2.7%.



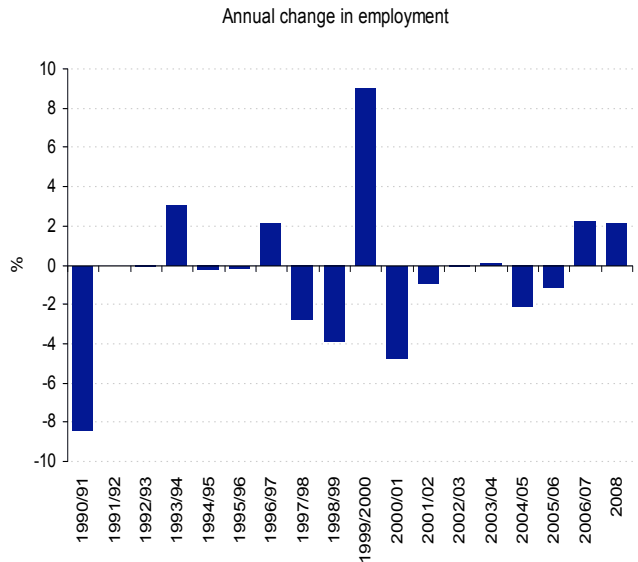
Sales are forecast to rise by 2.7% in volume terms ...

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Employment

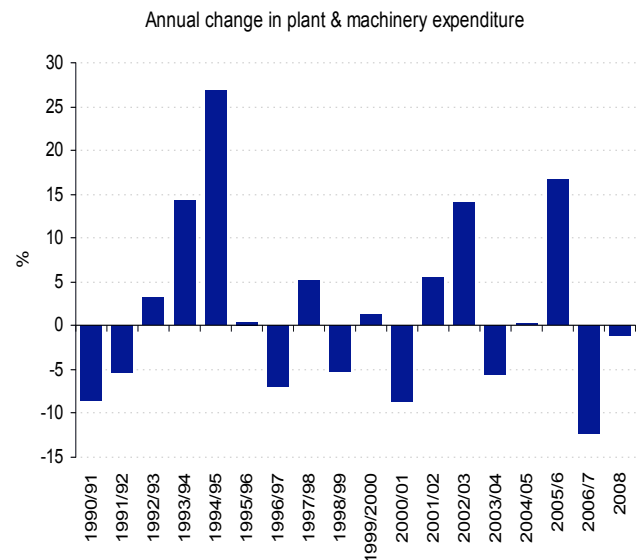
- Employment in manufacturing is forecast to rise by 2.2% in 2008, continuing the trend of the past year. In 2006/7, employment also rose by 2.2% in manufacturing (ABS).
- The forecast increase reflects both the expectation of positive domestic demand conditions, as well as the restructuring process in response to heightened global competition.
- Nevertheless, the employment forecast is optimistic, particularly if demand conditions do make an unexpected turn.



Employment is expected to rise by 2.2% ...

Investment in plant and machinery

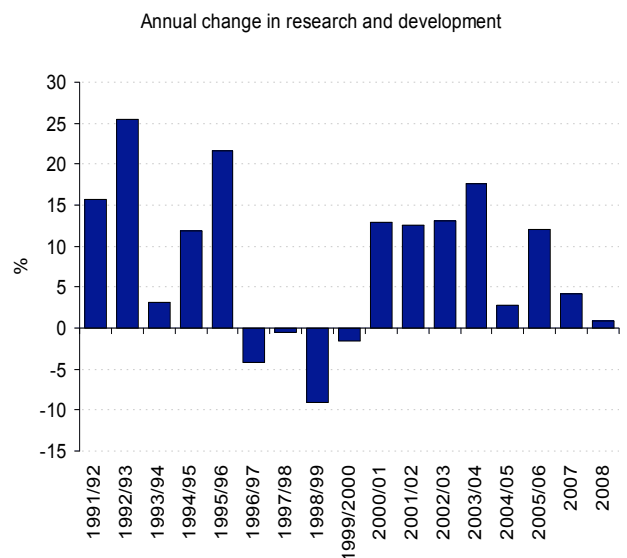
- Despite the positive sales conditions in 2006/7, ABS data shows there was a strong reduction in investment in new plant and equipment, a fall of 12.4%. However, this was after a surge in new investment in 2005/6.
- In 2008 investment in new plant and equipment is expected to continue to decline, by 1.2%.
- This is consistent with ABS forecasts that anticipate expenditure on new capital equipment in manufacturing will remain flat in 2008.



New investment spend forecast to decline by 1.2% ...

Research and development

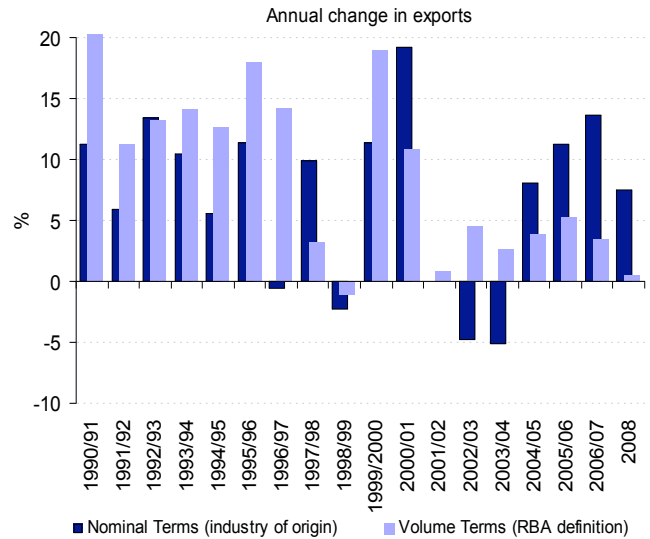
- The latest official ABS data for 2005/6 shows that research and development (R & D) spending by manufacturing rose by 12.0%.
- In 2007, along with the substantial reduction in investment spending, the forecast suggests that spending on R & D was also affected, with only a 4.2% increase expected.
- The forecast for 2008 is for a marginal increase in R & D expenditure (0.8%).



Research and development is anticipated to rise by 0.8% ...

Exports

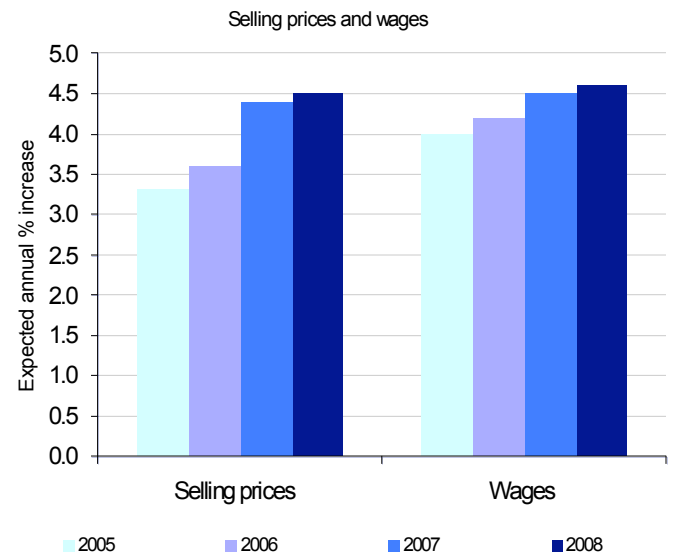
- In nominal terms, manufacturing exports rose relatively strongly in 2006/7, an increase of 13.7%, although in volume terms the increase was significantly smaller.
- Manufacturers are forecasting exports in nominal terms will rise by 7.5% in 2008. The Australian dollar is forecast to remain relatively strong for much of 2008, and this will impact on export growth.
- Adjusting for price movements, the impact of the Australian dollar will see exports in volume terms grow by just 0.5%, the weakest outcome in nine years.



Export volume growth forecast to rise by 0.5% ...

Selling prices and wages

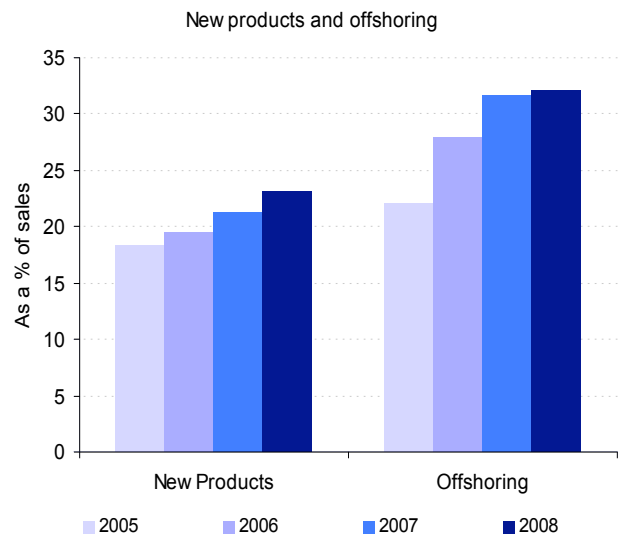
- Manufacturers expect selling prices to rise by 4.5% on average in 2008, a marginal increase on the 4.4% rise predicted for the previous year.
- The expectation for average wage growth in 2008 also rose marginally, lifting from 4.5% in 2007 to 4.6%.



Selling prices forecast to rise by 4.5% and wages by 4.6% ...

New products and offshoring

- Heightened global competition is placing increasing pressures on manufacturers to be more innovative and to make better use of global supply chains.
- New product intensity (the percentage of sales derived from new products introduced in the last three years) is expected to rise from 21.2% in 2007 to 23.1% in 2008.
- Offshoring can take two forms: companies moving part or whole of their operations overseas; and/or using a greater share of imported materials in domestic production. Both are seen as a major means of achieving cost reductions.
- The level of offshore intensity (offshore activity as a percentage of sales) is forecast to rise from 31.7% (revised) in 2007 to 32.0% in 2008.



New product development and offshoring to intensify ...

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