AUSTRALIAN PMI

PERFORMANCE OF MANUFACTURING INDEX®

AiGROUP

MEDIA CONTACT
Tony Melville
Australian Industry Group
Tel: 0419 190 347

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WEAK DOMESTIC DEMAND HITS MANUFACTURING

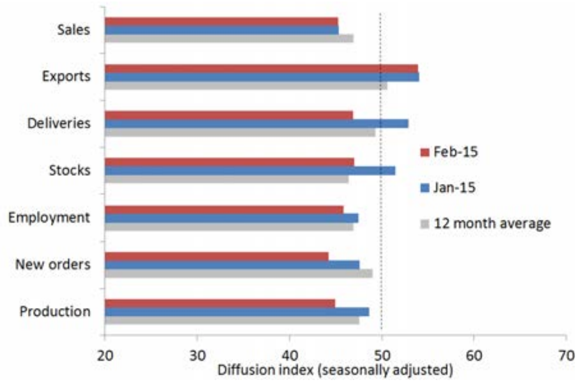
Australian PMI®	US Flash PMI	Markit Eurozone PMI	UK CIPS PMI	Japan Flash PMI	China Flash PMI
Feb 2015: 45.4 ↓	Feb 2015: **54.3** ↑	Feb 2015: **51.1** ↑	Jan 2015: **53.0** ↑	Feb 2015: **51.5** ↓	Feb 2015: **50.1** ↑

KEY FINDINGS

- The Australian Industry Group Australian Performance of Manufacturing Index **(Australian PMI®)** fell by 3.6 points to 45.4 points in February (seasonally adjusted). This indicated a third month of contraction in conditions (readings below 50 points indicate contraction) across the manufacturing sector following a brief stabilisation in November 2014.
- The **Australian PMI®** typically 'leads' ABS data for manufacturing output by around 3 months. Recent results from the **Australian PMI®** suggest manufacturing output (measured as 'value added' by the ABS) is likely to be broadly flat in Q4 2014 and so far in 2015.
- Manufacturing exports expanded for a third consecutive month in February, following further falls in the dollar. Much of this growth was concentrated in the food and beverages sub-sector.
- Among the other activity indicators however, manufacturing production contracted (i.e. below 50 points) for the fourth consecutive month while new orders declined for a third month. Manufacturing sales contracted for a ninth month in February. Supplier deliveries and stock levels also returned to contraction this month following a brief expansion in January, while manufacturing employment contracted for a second month.
- Three of the eight manufacturing sub-sectors in the **Australian PMI®** expanded (i.e. above 50 points) in February. The large food and beverages sub-sector expand for a ninth month, while the relatively small textiles, clothing and furniture sub-sector, and non-metallic mineral products (mainly building materials) both expanded for a fourth consecutive month.
- The lower Australian dollar and its further depreciation since September 2014 have boosted manufacturing export volumes over recent months. However, the lower dollar has also increased prices for imported inputs, which has put further downward pressure on manufacturers' margins. Despite the pickup in residential building over the past year, the sharp drop in mining construction, the progressive closure of automotive assembly, and weak local business investment, are weighing on demand for locally made machinery and components.

ACTIVITY SUB-INDEXES

- Manufacturing exports expanded for a third month in February, with this sub-index almost unchanged at 53.9 points (down 0.1 point). The lower Australian dollar and its further depreciation since September 2014 appears to have boosted manufacturing export volumes, with this sub-index expanding in eight out of the past 12 months. The 12-month moving average of the exports sub-index also moved into expansion, at 50.6 points this month, indicating a stronger long-term export trend.
- Less positively for the outlook, the new orders sub-index in the **Australian PMI®** declined by 3.4 points to 44.2 points in February. This signalled the third month of contraction in new orders.
- Meanwhile, manufacturing sales contracted for a ninth consecutive month, with the sales sub-index stable at 45.3 points in February. The production sub-index decreased by 3.7 points to 45.0 points in February, indicating a fourth month of contraction. Reflecting these weaker trading conditions, manufacturers reduced their supplier deliveries and stock levels in February following a brief expansion last month. The supplier deliveries sub-index dropped by 6.0 points to 46.9 points, while the stock (or inventories) sub-index fell by 4.4 points to 47.0 points in February.
- Manufacturing employment contracted for a second month in February. The employment sub-index decreased by 1.6 points to 45.9 points and last expanded in December 2014.
- Manufacturers' capacity utilisation rate declined slightly by 0.5 percentage points, with an average of 70.8% of total capacity being utilised across the manufacturing sector in February.

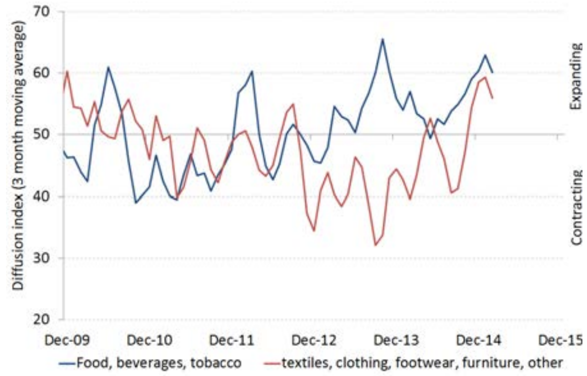


WAGES AND PRICES SUB-INDEXES

- The input prices sub-index of the **Australian PMI®** rose by 5.1 points to 72.4 points in February, well above the 12-month average of 65.2 points. This stronger increase in input prices likely reflected higher prices for imported inputs as the Australian dollar depreciated further.
- The wages sub-index increased by 1.8 points to 55.3 points in February. This suggests that annual manufacturing wages growth is likely to remain subdued in the 2015 March quarter following a 2.8% p.a. increase in Q4 2014 (according to ABS wage index data). This reflects ongoing weak labour demand in total (1.4% p.a. in Jan) and in manufacturing, as well as a rising unemployment rate (6.3% in Jan) and low background inflation (1.7% p.a. in Dec 2014).
- Manufacturing selling prices continued to contract this month, with the sub-index decreasing by 1.4 points to 48.3 points. This inability to raise selling prices continues to put downward pressure on manufacturers' margins, given the ongoing increases in input prices and wages.

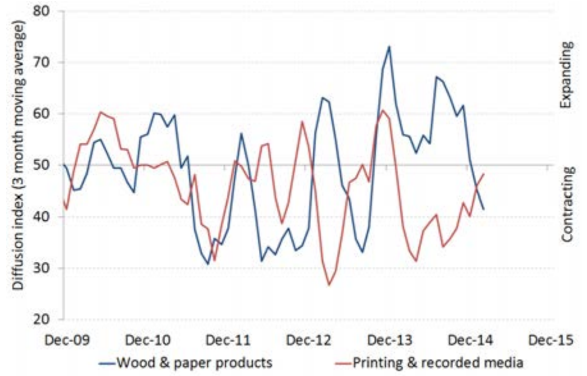
FOOD & BEVERAGES; TEXTILES, CLOTHING, FURNITURE & OTHER*

- The **food, beverages and tobacco sub-sector**'s index decreased by 2.8 points to 60.1 points in February (three-month moving averages). This indicated the ninth month of expansion for this sub-sector, after a brief contraction in May 2014. The food, beverages and tobacco sub-sector, the single largest manufacturing sub-sector, has recorded the strongest growth among all the manufacturing sub-sectors over the past two years. Local demand looks solid and export volumes are benefiting from a lower dollar, but respondents expressed concerns this month about a decline in global rural commodity prices and their potential effects in local markets.
- The small but very diverse **textiles, clothing, footwear, furniture and other manufacturing sub-sector** expanded for a fourth month in February, albeit at a slower pace. The sub-sector's index declined by 3.4 points to 56.0 points this month (three-month moving averages). The lower dollar, lower petrol prices and resurgent house building may have boosted local sales and export volumes for furniture and household goods, but fragile consumer sentiment continues to weigh on demand for Australian made clothing, footwear and personal products.



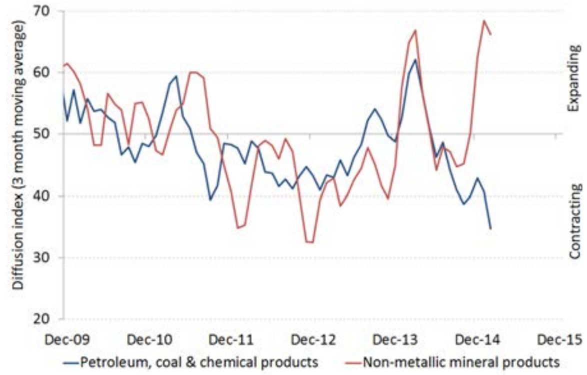
WOOD & PAPER; PRINTING & RECORDED MEDIA*

- The relatively small **wood and paper products sub-sector** contracted (i.e. below 50 points) for a second month in February. This followed expansion between October 2013 and November 2014. The sub-sector's index declined for a third month by 3.6 points in February to 41.5 points, the lowest level since September 2013 (three-month moving averages). Despite the pickup in house building activity and ongoing growth in food and beverages production, demand for wood-based building products and paper-based packaging products appear to have waned.
- The very small **printing and recorded media sub-sector**'s index increased by 2.2 points to 48.3 points (three-month moving averages), signalling the 14th consecutive month of contraction. Although the lower Australian dollar is reported to have boosted demand for locally made products, radical technology changes, soft business activity and ongoing intense import competition continue to dampen sales for locally printed products and recorded media.



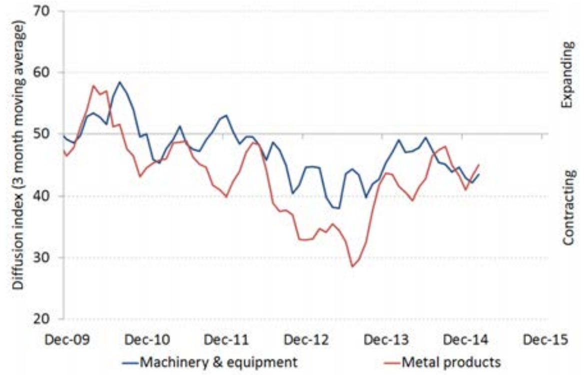
PETROLEUM, COAL & CHEMICALS; NON-METALLIC MINERALS*

- The **petroleum, coal, chemicals and rubber products sub-sector**'s index dropped by 6.0 points to 34.7 points in February (three-month moving averages). This indicated the ninth consecutive month of contraction (i.e. below 50 points) and the lowest reading since June 2009. Despite the lower dollar, the rapid decline in global oil prices, the ongoing decline of local mining construction activity, and the progressive closure of automotive assembly weighing on sales of Australian-made chemical inputs and components.
- The **non-metallic mineral products sub-sector**'s index declined by 2.3 points in February to 66.2 points (three-month moving average). This signalled a fourth consecutive month of expansion. The non-metallic mineral products sub-sector, which mainly produces building materials such as tiles, bricks, cement and glass, has benefitted from the improvement in residential building activity over the past year, with the RBA's cash rate cut in February and a lower Australian dollar further boosting confidence in this sub-sector.



METAL PRODUCTS; MACHINERY & EQUIPMENT*

- The very large **metal products sub-sector's** index moved up by 1.9 points to 45.0 points in February (three-month moving averages). This sub-sector has continued to contract since September 2010. Meanwhile, the index for the closely related **machinery and equipment sub-sector** increased by 1.4 points to 43.5 points (three-month moving averages). This important sub-sector, which includes automotive, other transport equipment, mining, agricultural, industrial and other specialist machinery and equipment, last expanded in January 2012.
- Respondents reported a general lack of new orders across the metal products and machinery and equipment sub-sectors in February. A lower Australian dollar has increased local demand and export volumes for locally made metal products and machinery and equipment, but it has also increased prices for imported inputs. Despite the benefits of stronger residential building activity over the past year, the sharp drop in resource construction, the progressive closure of Australian automotive assembly, and generally weak local business investment continue to weigh heavily on new orders and sales volumes. This has led to fierce competition among local metals and machinery businesses and further downward pricing pressures.



Seasonally adjusted	Index this month	Change from last month	12 month average		Index this month	Change from last month	12 month average
Australian PMI®	**45.4**	**-3.6**	**48.0**	**Exports**	53.9	-0.1	50.6
Production	45.0	-3.7	47.5	**Sales**	45.3	-0.1	46.9
New Orders	44.2	-3.4	49.0	**Input Prices**	72.4	5.1	65.2
Employment	45.9	-1.6	46.9	**Selling Prices (unadj.)**	48.3	-1.4	46.8
Inventories (stocks)	47.0	-4.4	46.4	**Average Wages (unadj.)**	55.3	1.8	56.6
Supplier Deliveries	46.9	-6.0	49.3	**Cap. Utilisation (%)(unadj.)**	70.8	-0.5	71.5

* All sub-sector indexes in the **Australian PMI®** are reported as three-month moving averages (3mma), so as to better identify the trends in these volatile monthly data.

What is the Australian PMI®? The Australian Industry Group **Australian Performance of Manufacturing Index (Australian PMI®)** is a seasonally adjusted national composite index based on the diffusion indices for production, new orders, deliveries, inventories and employment with varying weights. **An Australian PMI® reading above 50 points indicates that manufacturing is generally expanding; below 50, that it is declining.** The distance from 50 is indicative of the strength of the expansion or decline. Survey results are based on a rotating sample of around 200 manufacturing companies each month. New monthly seasonal adjustment factors were applied in April 2013. New industry classifications applied from December 2012 (and back-dated to 2009) based on the ANZSIC 2006 coding system and ABS 2011-12 industry weights.
For further economic analysis and information from the Australian Industry Group, visit http://www.aigroup.com.au/economics.
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