NAM MANUFACTURERS' OUTLOOK SURVEY
SECOND QUARTER 2017

July 20, 2017

Percentage of Respondents Positive in Their Own Company's Outlook **89.5%** *(March: 93.3%)* Small Manufacturers: **84.8%** *(March: 91.5%)* Medium-Sized Manufacturers: **90.6%** *(March: 93.8%)* Large Manufacturers: **92.8%** *(March: 93.9%)*	**NAM Manufacturing Outlook Index** **60.9** *(March: 63.5 – revised)* **Expected Growth Rate for SALES Over the Next 12 Months** **↑ 4.8%** *(March: ↑ 4.9%)*
Expected Growth Rate for PRODUCTION Over the Next 12 Months **↑ 4.8%** *(March: ↑ 4.8%)*	**Expected Growth Rate for EXPORTS Over the Next 12 Months** **↑ 1.1%** *(March: ↑ 1.0%)*
Expected Growth Rate for CAPITAL INVESTMENTS Over the Next 12 Months **↑ 3.2%** *(March: ↑ 2.1%)*	**Expected Growth Rate for PRICES Over the Next 12 Months** **↑ 1.7%** *(March: ↑ 1.8%)*
Expected Growth Rate for FULL-TIME EMPLOYMENT Over the Next 12 Months **↑ 2.7%** *(March: ↑ 2.3%)*	**Expected Growth Rate for INVENTORIES Over the Next 12 Months** **↑ 1.3%** *(March: ↑ 0.8%)*
Expected Growth Rate for EMPLOYEE WAGES Over the Next 12 Months **↑ 2.1%** *(March: ↑ 2.0%)*	**Expected Growth Rate for HEALTH INSURANCE COSTS Over the Next 12 Months** **↑ 8.4%** *(March: ↑ 7.2%)*
"Do you think the United States is headed in the right direction, or is our country on the wrong track?" **RIGHT TRACK: 56.9% WRONG TRACK: 14.3% UNSURE: 28.9%** *(March: Right Track: 59.9%, Wrong Track: 9.4%, Unsure: 30.8%)*	

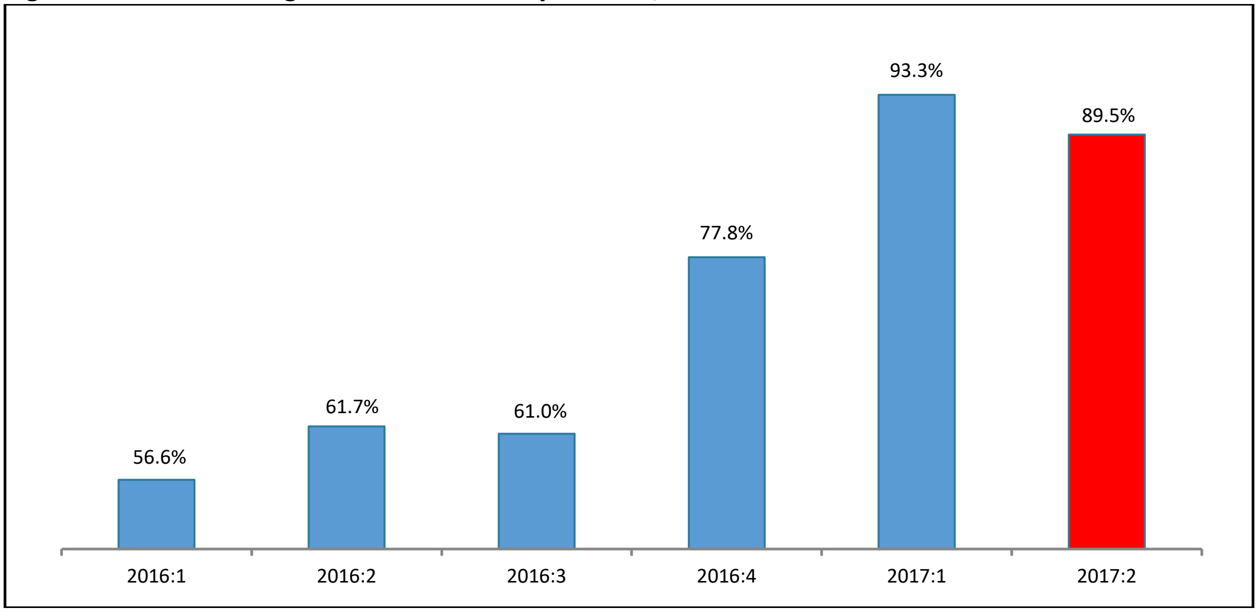
Summary

The manufacturing sector has begun to turn a corner in recent months, trending in the right direction both in the United States and globally after struggling for much of the past two years. In addition, there is a sense that many of the pro-growth policies that businesses have long sought, including tax reform, a major infrastructure package and regulatory relief, among others, might finally come to fruition, albeit perhaps slower than some might prefer. As a result, manufacturing leaders have shown increased optimism since the election. In March, the Manufacturers' Outlook Survey from the National Association of Manufacturers (NAM) rose to an all-time high in the survey's 20-year history, with 93.3 percent of respondents positive about their own company's outlook.

Three months later, manufacturers remain very upbeat. In the latest report, 89.5 percent were either somewhat or very positive about their own company's outlook (Figure 1). This pullback in confidence mirrors easing in other sentiment surveys, even as they continue to present an encouraging assessment of overall conditions. In this case, the percentage who are positive in their outlook has

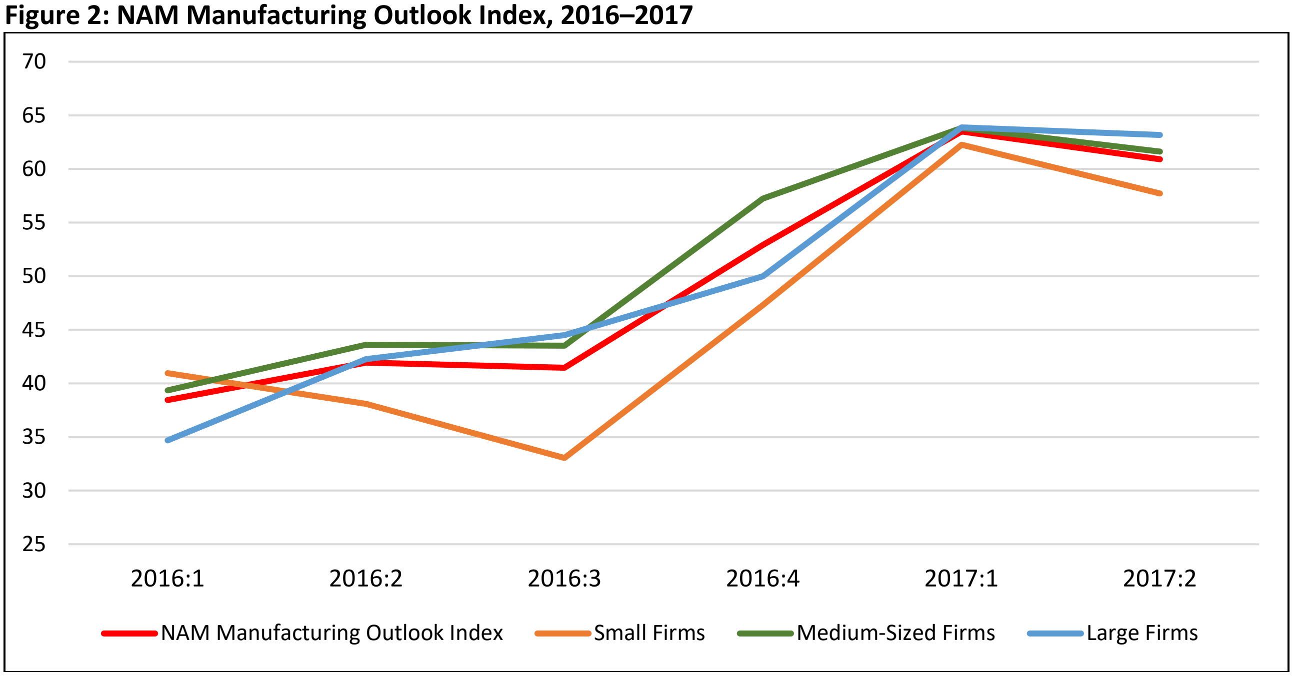
averaged 91.4 percent over the first and second quarters of 2017, the highest consecutive two-quarter average in the survey's history.

Figure 1: Manufacturing Business Outlook by Quarter, 2016–2017



Note: Percentage of respondents who characterized the current business outlook as somewhat or very positive

Figure 2: NAM Manufacturing Outlook Index, 2016–2017

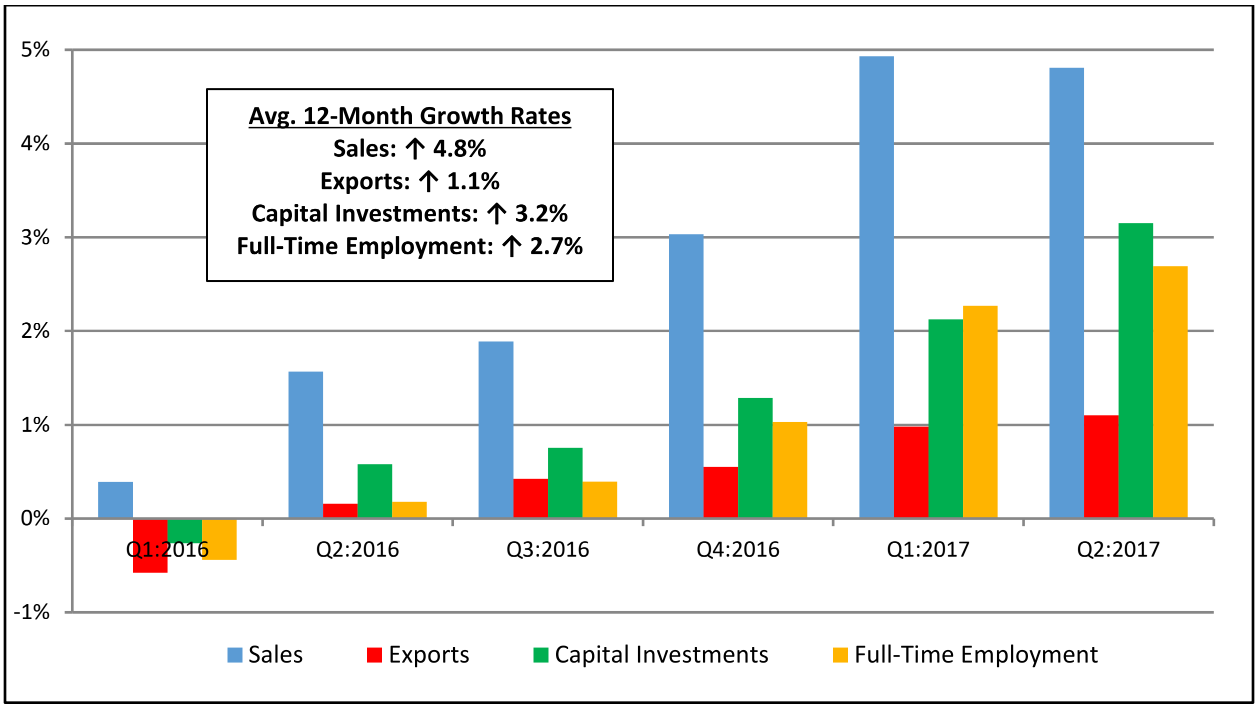


Source: National Association of Manufacturers

In a similar way, the NAM Manufacturing Outlook Index has also continued to be quite elevated, despite declining from 63.5 in March to 60.9 in June (Figure 2). Numbers over 60 indicate strong levels of optimism, with the percentage positive in their outlook more than one standard deviation from the historical average (73.5 percent positive). It was the third straight quarter where the outlook exceeded that average.

At the same time, while manufacturers are more positive in their outlook, it is also clear that they are grappling with new political uncertainties. A list of sample comments appears at the end of this report, with many respondents citing policy uncertainties in the new environment. Perhaps for that reason, a sizable proportion (28.9 percent) of respondents said that they were "unsure" when asked whether the United States was headed in the right direction. That measure has been highly volatile in the past three surveys. It is reassuring, though, that nearly 57 percent of respondents say that the country is headed in the right direction, with just 14.3 percent suggesting otherwise.

Figure 3: Expected Growth of Manufacturing Activity, 2016–2017



Note: Expected growth rates are annual averages.

Digging into the underlying data, recent improvements in sentiment have corresponded with stronger manufacturing activity – another sign that the sector is trending in the right direction. That is especially the case with hiring and capital spending plans, each of which is a good proxy of a firm's willingness to invest for the future. For instance, respondents are predicting that full-time employment will grow by 2.7 percent on average over the next 12 months, the fastest pace in the survey's history, up from 2.3 percent in the prior survey (Figure 3). Nearly 59 percent of manufacturers anticipate an increase in employment over the next year for their company, with one-quarter predicting a jump of at least 5 percent.

Similarly, firms forecast 3.2 percent growth in capital spending over the next 12 months, a six-year high and up from 2.1 percent in March. To illustrate this point, the percentage of respondents expecting capital expenditures to rise by at least 5 percent jumped from 25.5 percent three months ago to 35.9 percent today. Such a large jump in investment plans represents a healthy dose of confidence in the overall outlook. With that said, larger firms were more enthusiastic in capital spending plans than their smaller counterparts. Large manufacturers (i.e., those with 500 or more employees) expected to increase their capital spending by 3.6 percent on average over the next 12 months. Small businesses (i.e., those with less than 50 employees) suggested 2.6 percent growth moving forward.

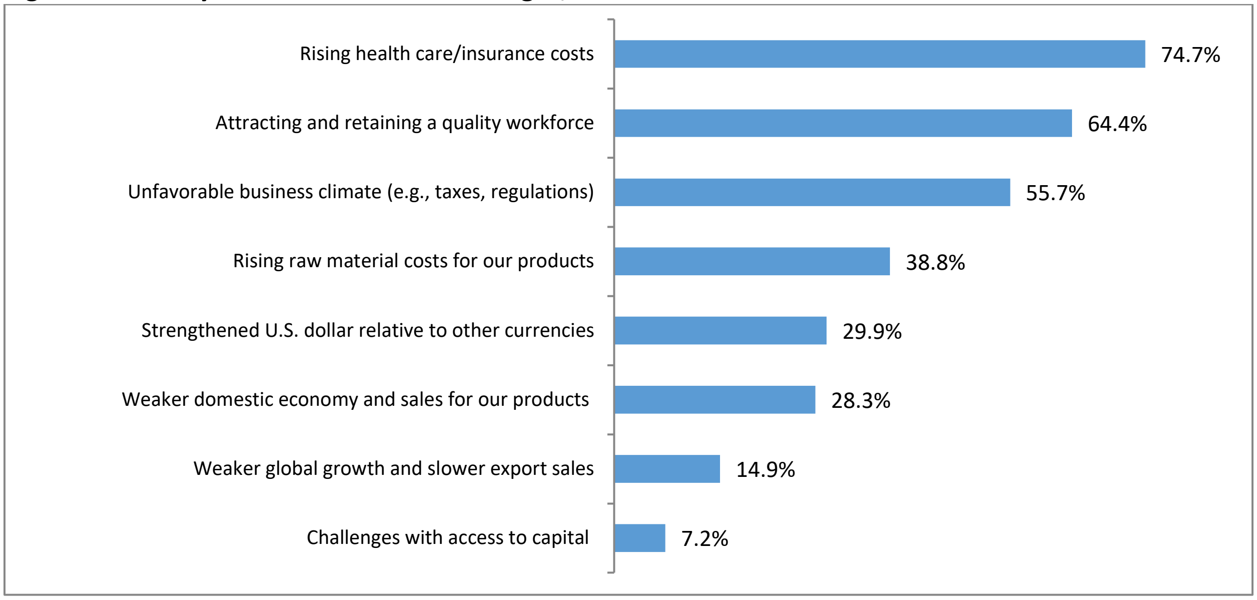
Much of this optimism stems from strong sales growth, which was little changed in this survey. Respondents are predicting sales growth of 4.8 percent on average over the next 12 months. This was off slightly from 4.9 percent expected growth in the prior release, which was the fastest pace in six years. Both figures represent a significant rebound from one year ago, with manufacturers forecasting 1.6 percent growth in the June 2016 report. In this survey, medium and larger firms (i.e., those with at least 50 employees) foresee expected sales growth of 5.0 percent for the next 12 months, with the smallest of manufacturers predicting an increase of 4.4 percent. The production data were similar, with 4.8 percent growth seen in the coming year, which is unchanged from the prior survey.

Export expectations have also moved in the right direction, which are notable given the challenges with increasing international demand due to global headwinds and a strong U.S. dollar. Respondents predict 1.1 percent growth in exports over the next 12 months, edging up from 1.0 percent in the prior survey and its highest rate since December 2014. One-third expect exports to increase over the next year, with 60.7 percent forecasting exports for their firm to be flat. Moreover, exports are once again an important determinant for the overall outlook of respondents. In particular, for those companies predicting a decline in exports over the next year, 61.7 percent were positive about their company's outlook, well below the 96.3 percent positive reading for those anticipating increased exports.

Meanwhile, manufacturers expect their inventories to grow by 1.3 percent over the next 12 months. This was the second consecutive increase in stockpiles after seven straight quarters of declines, and the pace was the fastest in 19 years. Just over 35 percent anticipate higher inventory stocks, with roughly half predicting no change. This is a reassuring development, consistent with the pickup in activity seen in other measures.

Rising health insurance cost were once again cited as a major concern, noted as their top business challenge by roughly three-quarters of the manufacturers completing the survey (Figure 4). They see these costs increasing 8.4 percent over the next year. More specifically, 75.2 percent expect their premiums to increase by at least 5 percent on average in the next year, with 39.9 percent predicting costs to rise by at least 10 percent. Small and medium-sized firms anticipate premiums to jump faster in the next year than large manufacturers do, at 8.8 percent and 7.5 percent, respectively.

Figure 4: Primary Current Business Challenges, Second Quarter 2017



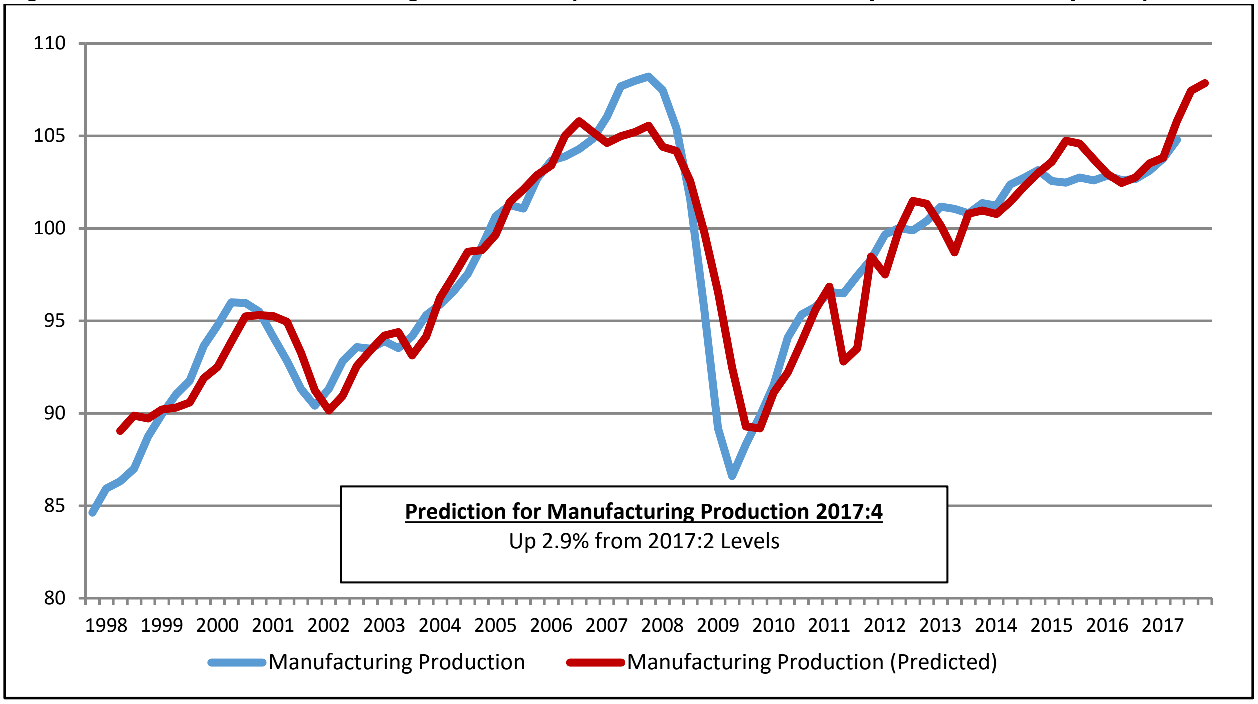
Note: Respondents were able to check more than one response; therefore, responses exceed 100 percent.

Respondents also listed attracting and retaining a quality workforce as a top worry, with 64.4 percent noting it as a primary challenge. The vast majority of those offering a comment about primary challenges for their business noted workforce development struggles, including frustrations with educational preparation, the work ethic of some candidates and the overall pool of qualified applicants. At the same time, the business environment fell to third place in the last survey, which is where it remained in this one. An unfavorable business climate was cited by 55.7 percent of those completing the survey, down from 71.2 percent and 58.2 percent in the past two releases, respectively. The likely reason for this drop is manufacturers' optimism that the new administration will continue to provide regulatory relief and make progress on regulatory and tax reform.

The current data suggest that manufacturing production should grow 2.9 percent between now and the fourth quarter of 2017 (Figure 5). As such, it would indicate that activity should continue to pick up in the coming months, with output in the sector currently growing 0.8 percent year-over-year. This finding comes from a regression model that explains nearly 90 percent of the variation in manufacturing production since the NAM Manufacturers' Outlook Survey began in the fourth quarter of 1997. In addition to the business outlook figure from this survey, the model includes current values for housing permits, the interest rate spread, personal consumption and the S&P 500.

Note that this is a fairly strong increase, well beyond the approximately 1.7 percent growth rate expected for manufacturing production in 2017. The positive impact of some variables, especially the stock market, likely weighed on the model's prediction. More than anything, it suggests continued movement in the right direction over the next six months.

Figure 5: Predicted Manufacturing Production (North American Industry Classification System)



Note: Industrial production is predicted two quarters in advance by regressing NAM Manufacturers' Outlook Survey data as one of the independent variables, with data stretching back to 1997:4. Other explanatory variables include current values for housing permits, the interest rate spread, personal consumption and the S&P 500.

Special Questions

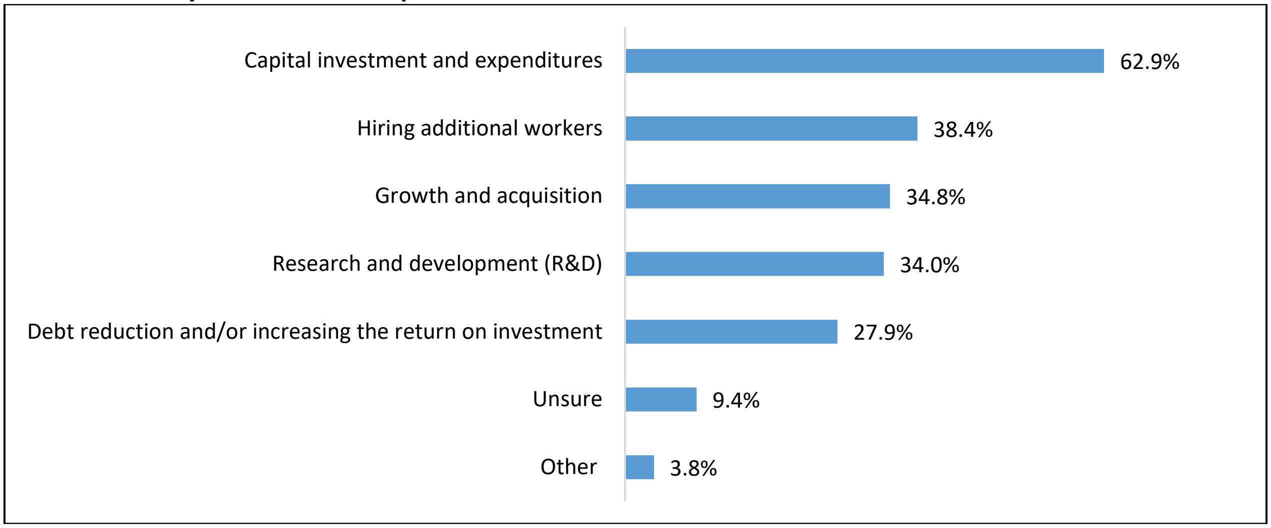
Reducing Regulatory Burdens

When asked, manufacturers have often cited rising cumulative regulatory burdens as one of their biggest concerns. With the exception of the last two quarters, the business climate was often listed as one of the top primary challenges in this survey. Indeed, 74.3 percent of respondents in this most recent survey said that their company's spending had increased either modestly or substantially over the past few years, with just 2.0 percent noting decreased spending. The perception that these burdens will be lessened has shifted concerns about the business climate to third place on the top challenges list in each of the past two surveys *(see above)*.

President Donald Trump has issued executive orders and presidential memoranda targeting the regulatory state, and the issuance of new regulations has slowed considerably. Manufacturers were asked about regulatory actions taken by the Trump administration so far, and 8 in 10 said that they approved of such moves, with 6.6 percent saying they disapproved and 12.9 percent unsure. More importantly, 57.1 percent felt that these actions aimed at reducing overall regulatory burdens would have a positive impact on their company's ability to expand, hire and spend more on capital equipment.

Along those lines, we asked firms how they might utilize the additional resources if the costs of regulatory compliance were reduced (Figure 6). Assuming funds were made available by reducing those costs, 62.9 percent said that they would use those dollars for increased capital investment and expenditures. In addition, those completing the survey said that they would also use those possible funds for hiring additional workers (38.4 percent), growth and acquisition (34.8 percent) and/or research and development (34.0 percent), among other options.

Figure 6: If the costs of regulatory compliance were reduced, how would your company most likely use the funds it formerly allocated to compliance?



Note: Respondents were able to check more than one response; therefore, responses exceed 100 percent.

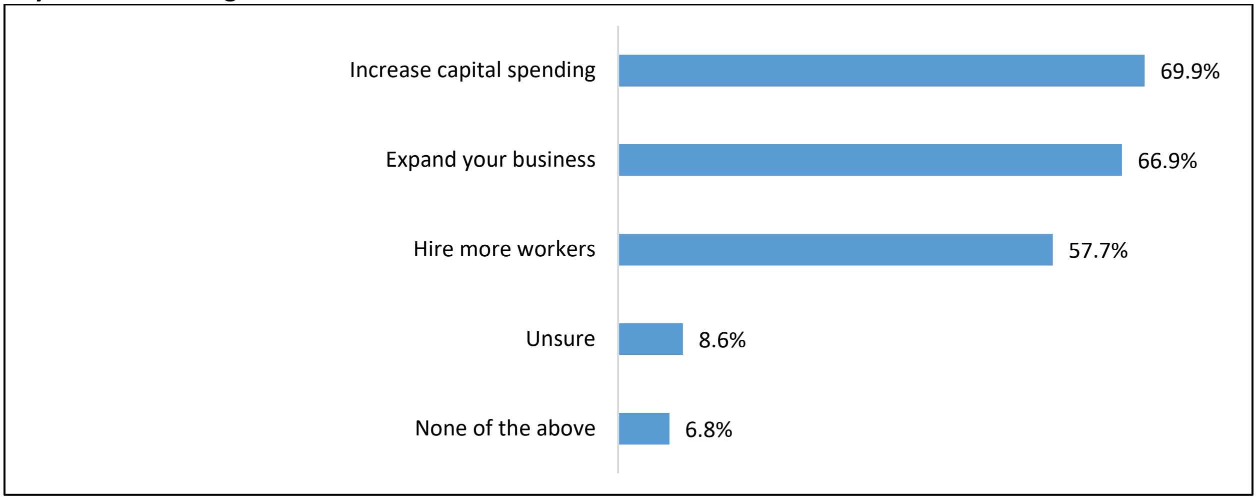
Enacting Comprehensive Business Tax Reform

Manufacturers are optimistic about the chance that long-sought-after comprehensive business tax reform will be enacted into law. The NAM's top priorities in tax reform include a corporate tax rate of 15 percent; comparable lower rates for pass-through businesses; a strong, permanent R&D incentive; robust capital cost-recovery rules; and a modern international tax system.

In this survey, nearly 87 percent of respondents said that a comprehensive plan that included these tax policy changes would address their concerns with the current tax system (Figure 7). Some respondents also included comments about state income taxes, individual tax rates, overall competitiveness relative to our trading partners, calls for fair treatment for small businesses and employee stock ownership plans (ESOPs) and a desire for revenue neutrality in any budget proposal, among others.

In general, the survey results and comments indicate support for a simpler and modern tax code that would allow manufacturers to be more competitive in the global marketplace. Along those lines, nearly 70 percent of respondents said that comprehensive business tax reform would encourage their company to increase capital spending (Figure 7). In addition, two-thirds suggested that it would enable them to expand their businesses, with 57.7 percent saying that they would hire more workers.

Figure 7: If comprehensive business tax reform is enacted, would it make your company more likely to do any of the following?



Note: Respondents were able to check more than one response; therefore, responses exceed 100 percent.

Note

This survey has been conducted quarterly since 1997, with the NAM's membership submitting this quarter's responses from May 18 to 30. In total, 906 manufacturers from all parts of the country, in a wide variety of manufacturing sectors and in varying size classifications, responded this quarter. Aggregated survey responses appear below. We expect the next survey in September.

Comments on Primary Challenges Facing Manufacturers

Respondents were given the opportunity to submit other challenges affecting their business aside from the choices given in the survey question. Here is a sample of the comments that were offered:

- "As our company is just under 2 years old. The company is growing more and more every day. Since this is happening, we are trying to get a loan so we can purchase a building so we can hire and grow easier without having space problems." *(Paper and paper products)*
- "Attracting employees that want to work and can pass the drug test." *(Plastics and rubber products)*
- "Finding candidates to hire is a `significant' issue even when the compensation and benefits are at a high level." *(Fabricated metal products)*
- "Grain prices affect our industry." *(Machinery)*
- "Infrastructure spending increases would be very beneficial." *(Other/Steel distribution)*
- "Lack of a quorum on Ex-Im Bank board that would enable them to finance transactions in excess of $10 million." *(Machinery)*
- "No balanced budget for the State of Illinois and a huge federal deficit with no balanced budget in sight." *(Fabricated metal products)*
- "No cooperation in Washington between the parties. No meaningful legislation without compromise." *(Fabricated metal products)*

- “The non-direct costs of manufacturing continue to rise. Things such as litigation protection, workers comp., general insurances.” *(Other/Textile manufacturing)*
- “Our industry suppliers and our customers are consolidating into larger companies.” *(Paper and paper products)*
- “Our international competition has lower taxes and regulations.” *(Fabricated metal products)*
- “Rail industry struggling due to drop in commodity volumes.” *(Chemicals)*
- “Regulations and high taxes are the most significant obstacles in front of us, along with the uncertainty of what will be done to alleviate these burdens.” *(Other/Heavy construction equipment)*
- “Retirement of key people without quality replacements to replace them.” *(Fabricated metal products)*
- “Rising steel prices is a significant problem in conjunction with inexpensive foreign competition.” *(Furniture and related products)*
- “Skills Gap!!!! We need real help rebuilding the apprenticeship infrastructure that existed decades ago.” *(Other/Tool and die and metal stamping)*
- “So much improvement has been started under President Trump - we need to keep it going to eliminate the high burdens on small businesses from the prior administration.” *(Machinery)*
- “There is good-sounding talk coming out of Washington on reducing regulatory burden, lowering taxes, etc., but not many solid actions/accomplishments yet.” *(Machinery)*
- “Unfair trade – i.e., Mexico purchasing raw material metals from China, and U.S. manufacturers cannot compete to manufacture finished goods at a competitive price!” *(Other/Tool and die and metal stamping)*

Survey Responses

1. How would you characterize the business outlook for your firm right now?
    a. Very positive – 27.3%
    b. Somewhat positive – 62.2%
    c. Somewhat negative – 9.3%
    d. Very negative – 1.1%

    Percentage that is either somewhat or very positive in their outlook = 89.5%

2. Over the next year, what do you expect to happen with your company's overall sales?
    a. Increase more than 10 percent – 22.9%
    b. Increase 5 to 10 percent – 29.9%
    c. Increase up to 5 percent – 25.8%
    d. Stay about the same – 14.2%
    e. Decrease up to 5 percent – 3.9%
    f. Decrease 5 to 10 percent – 2.0%
    g. Decrease more than 10 percent – 1.2%

    Average expected increase in sales consistent with these responses = 4.8%

3. Over the next year, what do you expect to happen with your company's overall production levels?
    a. Increase more than 10 percent – 21.9%
    b. Increase 5 to 10 percent – 30.4%
    c. Increase up to 5 percent – 25.4%
    d. Stay about the same – 16.3%
    e. Decrease up to 5 percent – 3.2%
    f. Decrease 5 to 10 percent – 1.7%
    g. Decrease more than 10 percent – 1.1%

    Average expected increase in production consistent with these responses = 4.8%

4. Over the next year, what do you expect to happen with the level of exports from your company?
    a. Increase more than 5 percent – 13.4%
    b. Increase 3 to 5 percent – 11.3%
    c. Increase up to 3 percent – 9.2%
    d. Stay about the same – 60.7%
    e. Decrease up to 3 percent – 2.7%
    f. Decrease 3 to 5 percent – 1.5%
    g. Decrease more than 5 percent – 1.2%

    Average expected increase in exports consistent with these responses = 1.1%

5. Over the next year, what do you expect to happen with prices on your company's overall product line?
    a. Increase more than 10 percent – 2.0%
    b. Increase 5 to 10 percent – 8.7%
    c. Increase up to 5 percent – 40.9%
    d. Stay about the same – 43.0%
    e. Decrease up to 5 percent – 4.9%
    f. Decrease 5 to 10 percent – 0.6%
    g. Decrease more than 10 percent – *none*

Average expected increase in prices consistent with these responses = 1.7%

6. Over the next year, what are your company's capital investment plans?
   a. Increase more than 10 percent – 19.5%
   b. Increase 5 to 10 percent – 16.4%
   c. Increase up to 5 percent – 19.2%
   d. Stay about the same – 36.7%
   e. Decrease up to 5 percent – 3.6%
   f. Decrease 5 to 10 percent – 2.0%
   g. Decrease more than 10 percent – 2.7%

   Average expected increase in capital investments consistent with these responses = 3.2%

7. Over the next year, what are your inventory plans?
   a. Increase more than 10 percent – 5.7%
   b. Increase 5 to 10 percent – 12.7%
   c. Increase up to 5 percent – 17.0%
   d. Stay about the same – 49.8%
   e. Decrease up to 5 percent – 10.0%
   f. Decrease 5 to 10 percent – 3.2%
   g. Decrease more than 10 percent – 1.7%

   Average expected increase in inventories consistent with these responses = 1.3%

8. Over the next year, what do you expect in terms of full-time employment in your company?
   a. Increase more than 10 percent – 8.1%
   b. Increase 5 to 10 percent – 17.2%
   c. Increase up to 5 percent – 33.6%
   d. Stay about the same – 35.9%
   e. Decrease up to 5 percent – 3.3%
   f. Decrease 5 to 10 percent – 0.9%
   g. Decrease more than 10 percent – 1.0%

   Average expected increase in full-time employment consistent with these responses = 2.7%

9. Over the next year, what do you expect to happen to employee wages (excluding nonwage compensation, such as benefits) in your company?
   a. Increase more than 5 percent – 4.4%
   b. Increase 3 to 5 percent – 24.5%
   c. Increase up to 3 percent – 58.0%
   d. Stay about the same – 12.5%
   e. Decrease up to 3 percent – 0.2%
   f. Decrease 3 to 5 percent – *none*
   g. Decrease more than 5 percent – 0.2%

   Average expected increase in employee wages consistent with these responses = 2.1%

10. Over the next year, what do you expect to happen to health insurance costs for your company?
   a. Increase 15.0 percent or more – 14.7%
   b. Increase 10.0 to 14.9 percent – 25.2%
   c. Increase 5.0 to 9.9 percent – 35.3%
   d. Increase less than 5.0 percent – 15.0%

e. No change – 6.2%
f. Decrease less than 5.0 percent – 0.3%
g. Decrease 5.0 percent or more – 0.2%
h. Uncertain – 3.1%

Average expected increase in health insurance costs consistent with these responses = 8.4%

11. Do you think the United States is headed in the right direction, or is our country on the wrong track?
    a. Right direction – 56.9%
    b. Wrong track – 14.3%
    c. Unsure – 28.9%

12. What are the biggest challenges you are facing right now? *(Check all that apply.)*
    a. Weaker domestic economy and sales for our products to U.S. customers – 28.3%
    b. Weaker global growth and slower export sales – 14.9%
    c. Strengthened U.S. dollar relative to other currencies – 29.9%
    d. Challenges with access to capital or other forms of financing – 7.2%
    e. Unfavorable business climate (e.g., taxes, regulations) – 55.7%
    f. Increased raw material costs – 38.8%
    g. Rising health care/insurance costs – 74.7%
    h. Attracting and retaining a quality workforce – 64.4%

13. What is your company's primary industrial classification?
    a. Chemicals – 4.9%
    b. Computer and electronic products – 1.6%
    c. Electrical equipment and appliances – 3.8%
    d. Fabricated metal products – 32.7%
    e. Food manufacturing – 3.0%
    f. Furniture and related products – 1.1%
    g. Machinery – 11.2%
    h. Nonmetallic mineral products – 1.8%
    i. Paper and paper products – 3.0%
    j. Petroleum and coal products – 0.7%
    k. Plastics and rubber products – 8.4%
    l. Primary metals – 3.4%
    m. Transportation equipment – 3.1%
    n. Wood products – 2.6%
    o. Other – 18.8%

14. What is your firm size (e.g., the parent company, not your establishment)?
    a. Fewer than 50 employees – 24.5%
    b. 50 to 499 employees – 56.7%
    c. 500 or more employees – 18.8%

<u>SPECIAL QUESTIONS</u>

Reducing Regulatory Burdens

15. Do you approve of the regulatory actions taken to date by the Trump administration?
    a. Yes – 80.5%
    b. No – 6.6%
    c. Unsure – 12.9%

16. Do the president's regulatory policies make your company more likely to expand your business, including more hiring and capital spending?
    a. These actions will have a positive impact on my company's expansion, hiring and capital spending plans – 57.1%
    b. It will have no impact on my company's expansion, hiring and capital spending plans – 23.2%
    c. These actions will have a negative impact on my company's expansion, hiring and capital spending plans – 2.7%
    d. Unsure – 16.9%

17. Prior to 2017, how has your company's total spending on state and federal regulatory compliance changed over the past few years?
    a. Decreased substantially – 0.9%
    b. Decreased modestly – 1.1%
    c. Not changed – 21.1%
    d. Increased modestly – 41.8%
    e. Increased substantially – 32.5%
    f. Unsure – 2.6%

18. If the costs of regulatory compliance were reduced, how would your company most likely use the funds it formerly allocated to compliance? *(Check all that apply.)*
    a. Capital investment and expenditures – 62.9%
    b. Hiring additional workers – 38.4%
    c. Growth and acquisition – 34.8%
    d. Research and development (R&D) – 34.0%
    e. Debt reduction and/or increasing the return on investment – 27.9%
    f. Other – 3.8%
    g. Unknown – 9.4%

Enacting Comprehensive Business Tax Reform

19. The NAM's top priorities in tax reform include a corporate tax rate of 15 percent, comparable lower rates for pass-through businesses, a strong, permanent R&D incentive, robust capital cost-recovery rules and a modern international tax system. Do these priorities for comprehensive business tax reform address your concerns with the current tax system?
    a. Yes – 86.6%
    b. No – 5.2%
    c. Unsure – 8.2%

20. If comprehensive business tax reform is enacted along the lines described in the previous question, would it make your company more likely to do any of the following? *(Check all that apply.)*
    a. Expand your business – 66.9%
    b. Hire more workers – 57.7%
    c. Increase capital spending – 69.9%
    d. None of the above – 6.8%
    e. Unsure – 8.6%