NAM Manufacturers' Outlook Survey

Manufacturing Outlook

PERCENTAGE OF RESPONDENTS POSITIVE IN THEIR OWN COMPANY'S OUTLOOK

61.7%

(March: 56.6%)

Small Manufacturers: 56.1% (March: 60.3%)
Medium-Sized Manufacturers: 64.2% (March: 57.9%)
Large Manufacturers: 62.2% (March: 51.1%)

NAM MANUFACTURING OUTLOOK INDEX

42.2

(March: 38.7)

Expected Growth Rate Over the Next 12 Months

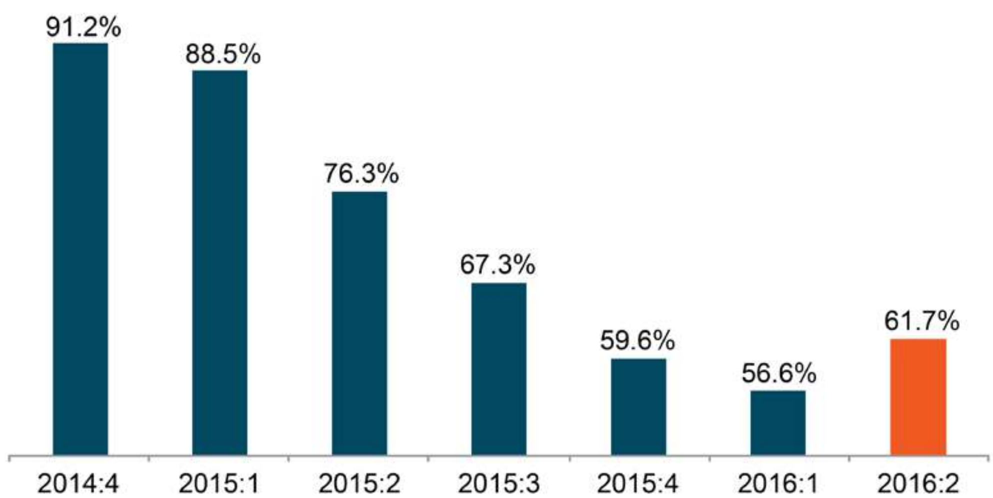
SALES	Up 1.6%	(March: Up 0.4%)
PRODUCTION	Up 1.5%	(March: Up 0.5%)
EXPORTS	Up 0.2%	(March: Down 0.6%)
CAPITAL INVESTMENTS	Up 0.6%	(March: Down 0.3%)
PRICES	Up 0.6%	(March: Up 0.02%)
FULL-TIME EMPLOYMENT	Up 0.2%	(March: Down 0.4%)
INVENTORIES	Down 1.0%	(March: Down 1.5%)
EMPLOYEE WAGES	Up 1.5%	(March: Up 1.1%)
HEALTH INSURANCE COSTS	Up 8.3%	(March: Up 7.6%)

Summary

The latest National Association of Manufacturers (NAM) quarterly survey continued to reflect concerns over continuing economic challenges. However, it also issued rays of encouragement, particularly after the pullbacks in activity seen in the prior release. In this survey, 61.7 percent of manufacturers are either somewhat or very positive about their own company's outlook, up from 56.6 percent who said the same thing in March (Figure 1). It also ends a five-quarter slide in confidence, down from 91.2 percent in the fourth quarter of 2014, suggesting that respondents are somewhat more upbeat today than three months ago. In that way, the NAM survey responses mirror the stabilization seen in the Institute for Supply Management's reports, with manufacturing expanding now for three straight months.

Despite some progress in this quarter's data, the NAM Manufacturing Outlook Index remains below 50, the level consistent with the survey's historical mean of 73.2 percent, rising from 38.7 to 42.2 (Figure 2). Medium-sized manufacturers (i.e., those with between 50 and 499 employees) or larger (i.e., those with 500 or more employees) are more upbeat in their company's outlook than their smaller counterparts (i.e., those with fewer than 50 employees), with confidence ranging from 56.1 percent positive for small manufacturers to 64.2 percent for mid-market firms.

Figure 1: Manufacturing Business Outlook by Quarter, Fourth Quarter 2014 – Second Quarter 2016



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

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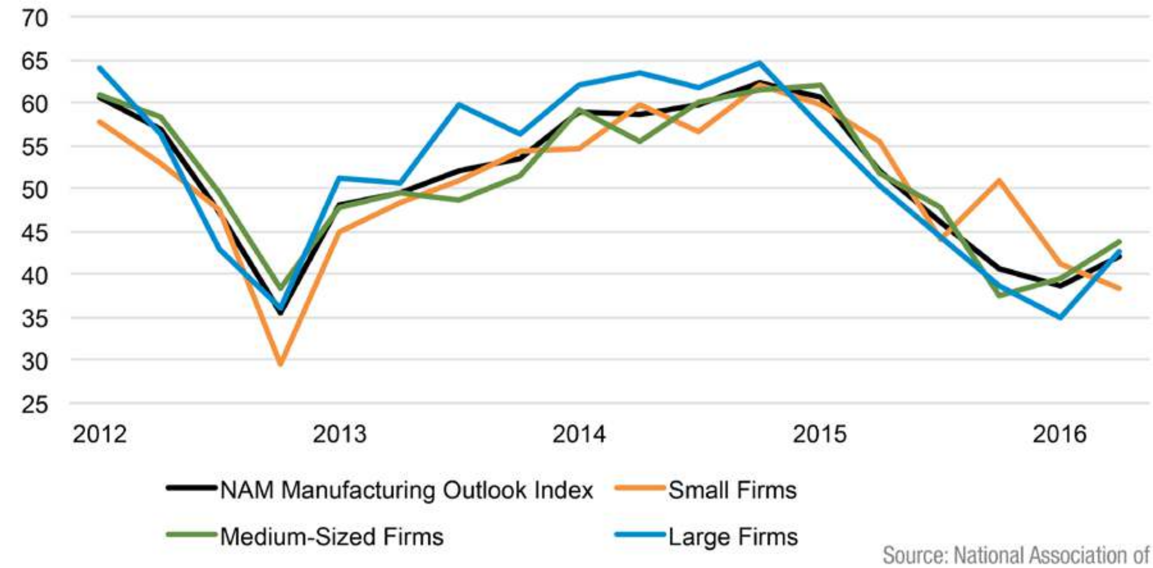
Figure 2: NAM Manufacturing Outlook Index, 2012–2016



Source: National Association of Manufacturers.

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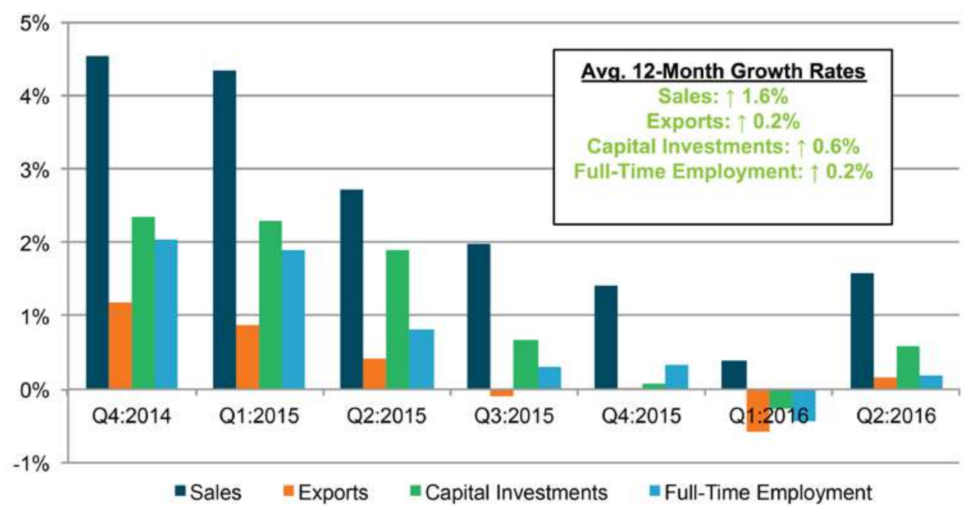
The outlook for smaller businesses is lower in this survey than in March, but the other two categories improved. What is interesting about that result is that sales expectations are inversely related to size, with smaller firms predicting 1.9 percent growth in sales over the next 12 months versus 1.5 percent for medium-sized and larger manufacturers. Yet, as with the past few surveys, the numbers are highly correlated with trade data. Of those companies that anticipate increased exports over the next 12 months, 81.0 percent are positive in their outlook in this survey. In contrast, the positive outlook of respondents expecting their imports to remain the same fell to 64.8 percent; only 28.3 percent have a positive outlook among those predicting decreased exports over the next year. Overall, respondents expect exports to increase 0.2 percent over the next 12 months, improving from an expected decline of 0.6 percent in the prior survey.

Figure 3: Expected Growth of Manufacturing Activity, Fourth Quarter 2014 – Second Quarter 2016



Note: Expected growth rates are annual averages.

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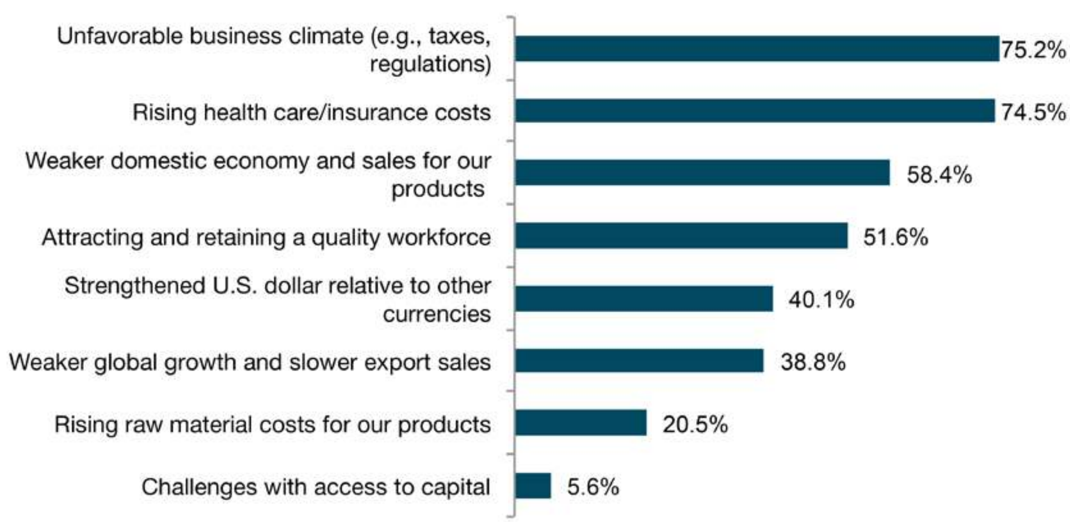
Beyond exports, there were also better data for most of the other key data points on expected activity, including sales. Manufacturers anticipate sales to grow 1.6 percent over the next 12 months, up from 0.4 percent in March but down sharply from 4.5 percent in December 2014 (Figure 3). In this survey, 52.4 percent of respondents expect sales to increase over the next year, up from 41.9 percent who said the same thing three months ago. Roughly one-quarter do not anticipate any change in demand moving forward. Production numbers are similar, with business leaders expecting 1.5 percent growth over the next 12 months, up from 0.5 percent in March's survey.

With a pickup in demand, businesses are more comfortable in their hiring and capital spending plans, according to this survey. Full-time employment levels are expected to grow 0.2 percent over the next year, an improvement from the decline of 0.4 percent noted in the prior release. More than 30 percent anticipate hiring increases in the next 12 months, with 26.4 percent predicting declining employment. Small and medium-sized firms expect hiring to grow 0.4 percent moving forward, whereas larger firms predict a decline of 0.6 percent on average over the next year. On this latter point, 40.2 percent of large manufacturers think that employment will fall in the months ahead, compared to 23.2 percent seeing increases.

Interestingly, capital investment plans are the opposite, with smaller entities shrinking their capital spending plans 0.1 percent but medium-sized and large manufacturers predicting increases of 0.7 percent. Among all firms, expected capital expenditures over the next year improved from a decline of 0.3 percent in March to a gain of 0.6 percent in June. Almost 36 percent anticipate capital spending to increase over the next year, up from 31.2 percent who said the same thing in the previous survey. If orders and production continue to improve, we would expect respondents to be more willing to add workers and invest in capital equipment in upcoming surveys.

Meanwhile, manufacturers expect their inventories to decrease 1.0 percent over the next 12 months, declining for the fifth straight quarter. In this survey, 36.6 percent anticipate declining inventory stocks, with 17.0 percent predicting increases. There is a silver lining from declining inventory stocks. If demand picks up significantly, manufacturing output would have to accelerate substantially to match the increased sales.

Figure 4: Primary Current Business Challenges, Second Quarter 2016



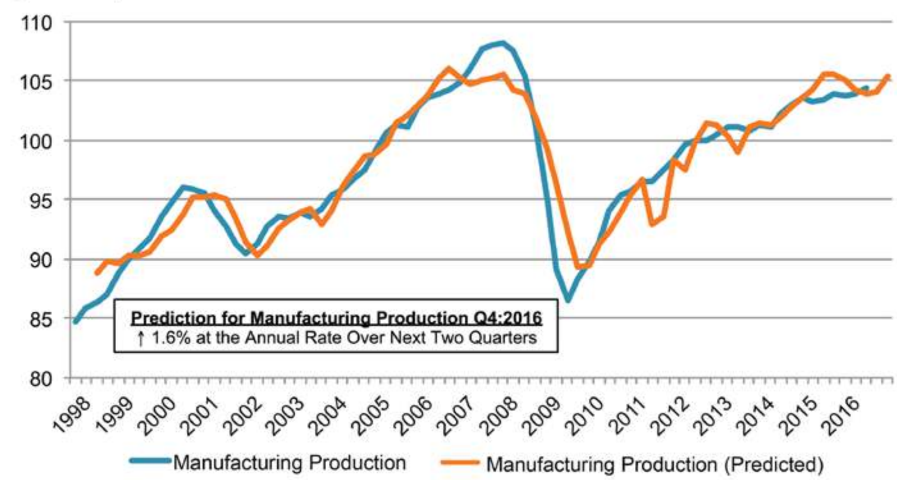
Note: Respondents were able to check more than one response; therefore, responses exceed 100 percent.

Respondents cited an unfavorable business climate as their top business challenge (Figure 4), with three-quarters of manufacturers noting tax and regulatory concerns as being first and foremost on their minds. Indeed, manufacturers continue to be frustrated with the lack of comprehensive tax reform and with a perceived regulatory assault on their businesses. Many respondents noted their concerns on these issues. Along those lines, 75.4 percent believe the United States is on the wrong track, with 8.2 percent feeling we are headed in the right direction. The remainder are unsure. On the positive side, this reflects an improvement from the prior survey, which had the right track and wrong track numbers at 3.7 percent and 85.6 percent, respectively.

Health insurance costs are also a major challenge for businesses in this survey, cited by 74.5 percent of respondents. Manufacturers see health insurance costs increasing 8.3 percent over the next 12 months, up from 7.6 percent in the prior release. More specifically, 76.9 percent expect their premiums to increase by at least 5 percent on average in the next year, with 35.6 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 8.9 percent and 6.7 percent, respectively.

The current data suggest that manufacturing production should grow 1.6 percent at the annual rate over the next two quarters (Figure 5). As such, it would indicate that activity should continue to pick up in the coming months. Nonetheless, growth will remain more subdued than we might desire. This finding comes from a regression model that explains more than 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.

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



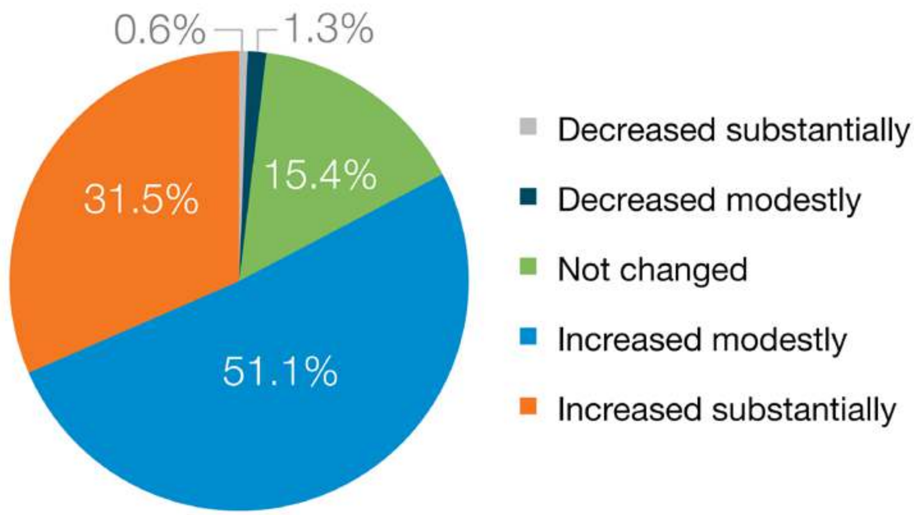
Note: Industrial production is predicted two quarters in advance by regressing NAM Manufacturers' Outlook Survey data as one of the independent variables, with data stretching back to Q4:1997. Other explanatory variables include current values for housing permits, the interest rate spread, personal consumption and the S&P 500.

Special Questions

Regulatory Burdens

As noted earlier, regulatory burdens continue to be one of the primary challenges cited by three-quarters of respondents. We wanted to dig a little deeper into this issue to get a better sense of how costs associated with regulatory compliance impact manufacturing operations. The data tend to confirm the notion that cumulative regulatory burdens keep getting larger. For instance, 82.6 percent of respondents said their company's total spending on state and federal regulatory compliance had increased either modestly or substantially over the past few years (Figure 6). Only about 15 percent cited no change in their regulatory spending, with 1.9 percent noting decreases. More specifically, the typical manufacturer said it devotes 4.3 percent of its total expenditures to regulatory compliance, with 31.8 percent who responded saying that compliance costs exceed 5 percent of total expenditures.

Figure 6: How Has Your Company's Total Spending on State and Federal Regulatory Compliance Changed Over the Past Few Years?



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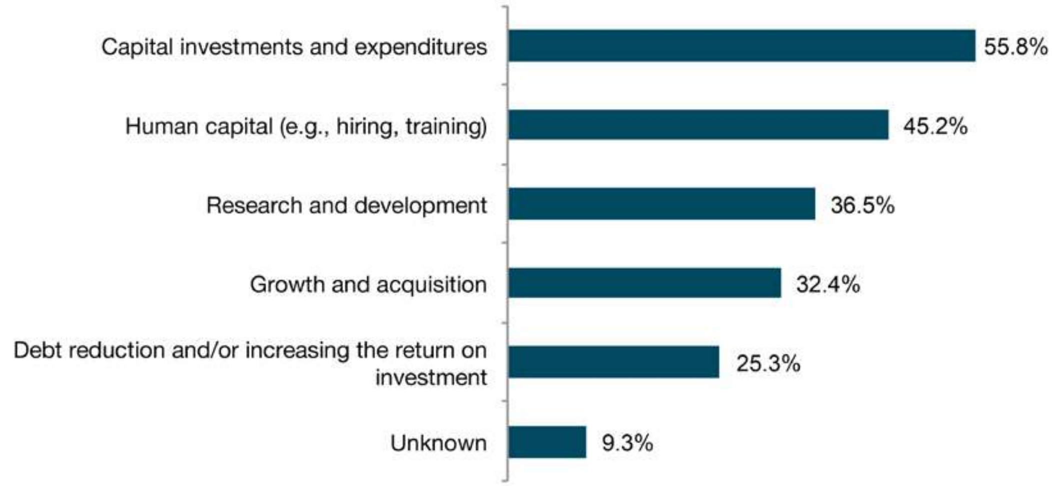
It should be said that manufacturers are not anti-regulation, as they recognize that rules are put in place to help protect the environment, provide a safe workplace and ensure fairness in competition. Yet, the cumulative burden of ever-increasing regulations does come at a cost.

At the end of the day, the time and dollars devoted to complying with state and federal rules mean that businesses cannot use those resources for other endeavors. We asked respondents about the opportunity costs of those dollars, assuming regulatory burdens were reduced somewhat, and the results suggest that manufacturing leaders would use those funds to grow their firms if given the chance. Respondents said they would devote more dollars to capital investments and expenditures (55.8 percent), human capital (45.2 percent), research and development (R&D) (36.5 percent), growth and acquisition (32.4 percent) and debt reduction and/or increasing the return on investments (25.3 percent).

Figure 7: If the Cost 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.

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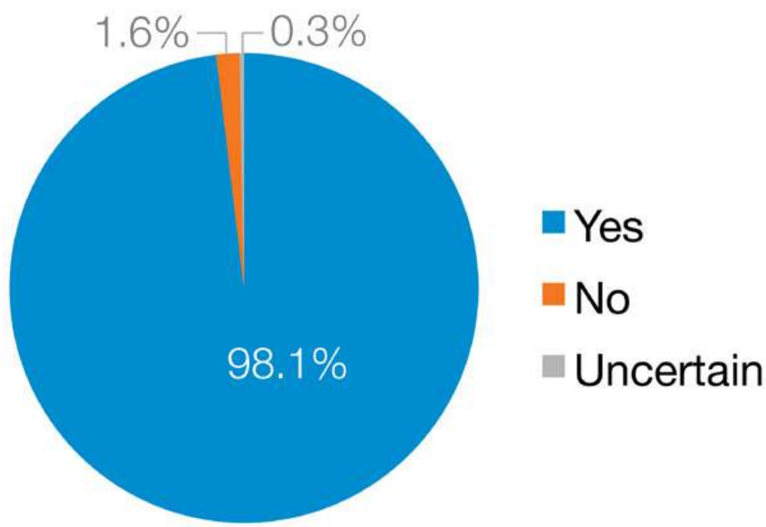
Figure 8: Does Your Company Provide Health Benefits to Your Employees?



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Health Insurance

Rising health insurance costs continue to be one of the top challenges for manufacturers, as noted earlier. Almost three-quarters of respondents said this is a primary challenge for their business, with premium costs expected to rise 8.3 percent over the next 12 months in this survey. Despite the concerns about ever-higher costs, manufacturers continue to see value in providing health benefits to their employees, especially as a recruitment tool for attracting talent. In fact, 98.1 percent said they provide health insurance to their workers, with just 1.6 percent saying they do not (Figure 8).

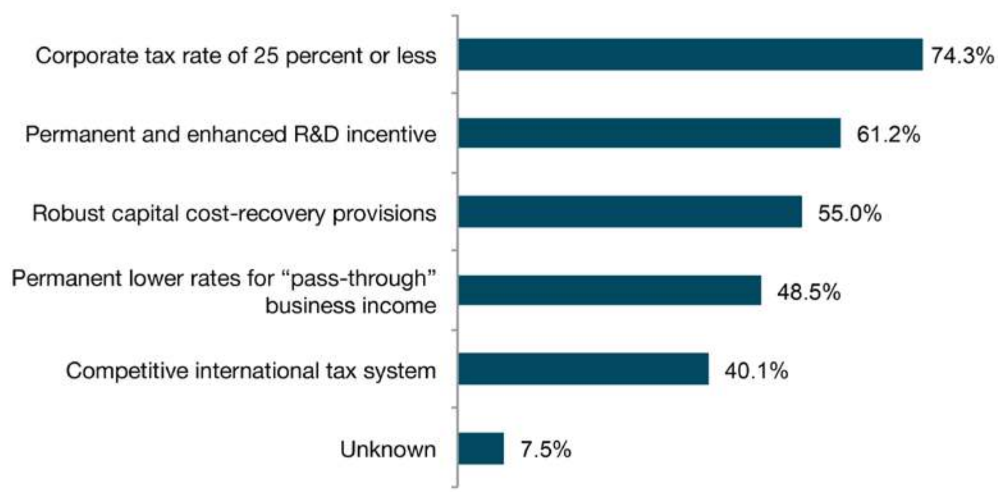
Tax Reform

The NAM has long called for comprehensive business tax reform that lowers corporate tax rates to 25 percent or less, includes a robust capital cost-recovery system and a permanent R&D incentive, moves to a modern international tax system and includes lower tax rates for "pass-through" manufacturers. As the tax debate moves forward, there is growing interest in comprehensive business tax reform that includes lower tax rates for corporations and for business income earned by "pass-through" entities. The individual tax code would remain essentially the same. With this in mind, we asked a series of questions to gauge interest in comprehensive business tax reform.

The first question asked respondents how their company is organized. Of those responding, 51.8 percent are organized as "pass-through" entities (e.g., a subchapter S corporation, a partnership). "Pass-through" entities then were asked if they support comprehensive business tax reform that includes lower tax rates. Nearly 77 percent said they support comprehensive business tax reform along those lines, with just 4.7 percent suggesting they do not support it. In addition, 18.5 percent are uncertain.

Finally, we asked all respondents whether specific proposals discussed as part of comprehensive business tax reform, if enacted, would make them more competitive. Almost three-fourths of respondents (74.3 percent) said a corporate tax rate of 25 percent or less would make them more competitive, with a permanent and enhanced R&D incentive cited by 61.2 percent, robust capital cost-recovery provisions by 55.0 percent, permanent lower rates for "pass-through" business income by 48.5 percent and a competitive international tax system by 40.1 percent (Figure 9). Respondents were able to select more than one reply.

Figure 9: Would Your Business Be More Competitive if the Following Policies Were Enacted as Part of Tax Reform?



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

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The responses differed depending on the form of business organization. For instance, "pass-through" entities are more likely to support a permanently lower rate for themselves (76.0 percent), which is not surprising. Likewise, non-"pass-through" entities—most likely C corporations—are more likely to suggest that reduced corporate tax rates (84.7 percent), a permanent and enhanced R&D incentive (67.2 percent), robust capital cost-recovery provisions (58.4 percent) and a competitive international tax system (49.6 percent) would make them more competitive.

Note

This survey has been conducted quarterly since 1997, with the NAM's membership submitting this quarter's responses from May 13 to May 31. In total, 322 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. The next survey is expected to be released on Wednesday, September 7, 2016.

Sample Comments on Primary Challenges Facing Manufacturers

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

"China slowdown." (Textiles)

"Cost of doing business in Hawaii is increasing, including trucking and shipping and state taxes and regulations." (Plastics and rubber products)

"Customer's low-cost sourcing strategies." (Fabricated metal products)

"End-market softness in transportation, agriculture and mining sectors." (Other)

"The ever-more burdensome regulatory environment needs to be emphasized. The risk/reward balance is completely out of whack." (Chemicals)

"Federal-mandated wage increases." (Machinery)

"Finding the courage to make major investments in our business." (Machinery)

"Global competition for our markets. Mandated state and city minimum wage and paid sick leave changes in California and Los Angeles." (Aerospace and other transportation equipment)

"High level of imports and weak prices in the energy sector." (Primary metals)

"Imports from India and China. Unfair trade policy." (Primary metals)

"International competition/imports." (Plastics and rubber products)

"Low commodity prices." (Petroleum and coal products)

"Minimum wage increases." (Computer and electronic products)

"Oil price impacts." (Transportation equipment)

"Regulations in almost every segment have become an impediment for growth and investment." (Other)

"Regulatory barriers to various export markets." (Medical diagnostics manufacturing)

"Two concerns: 1. aging current workforce equals lost knowledge, increased insurance utilization, succession planning, etc., and 2. lack of 'blue collar' manufacturing interest within the younger workforce population." (Fabricated metal products)

"Uncertainty and competence of presidential nominees." (Machinery)

Survey Responses

1. How would you characterize the business outlook for your firm right now?

a. Very positive – 10.6%
b. Somewhat positive – 51.1%
c. Somewhat negative – 33.0%
d. Very negative – 5.3%

Percentage that is either somewhat or very positive in their outlook = 61.7%

2. Over the next year, what do you expect to happen with your company's overall sales?

a. Increase more than 10 percent – 7.5%
b. Increase 5 to 10 percent – 18.4%
c. Increase up to 5 percent – 26.5%
d. Stay about the same – 24.6%
e. Decrease up to 5 percent – 11.8%
f. Decrease 5 to 10 percent – 7.8%
g. Decrease more than 10 percent – 3.4%

Average expected increase in sales consistent with these responses = 1.6%

3. Over the next year, what do you expect to happen with your company's overall production levels?

a. Increase more than 10 percent – 7.5%
b. Increase 5 to 10 percent – 16.9%
c. Increase up to 5 percent – 26.6%
d. Stay about the same – 25.4%
e. Decrease up to 5 percent – 13.2%
f. Decrease 5 to 10 percent – 6.3%
g. Decrease more than 10 percent – 4.1%

Average expected increase in production consistent with these responses = 1.5%

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 – 7.6%
b. Increase 3 to 5 percent – 7.9%
c. Increase up to 3 percent – 9.8%
d. Stay about the same – 54.9%
e. Decrease up to 3 percent – 7.0%
f. Decrease 3 to 5 percent – 6.0%
g. Decrease more than 5 percent – 6.7%

Average expected increase in exports consistent with these responses = 0.2%

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 – 0.9%
b. Increase 5 to 10 percent – 2.5%
c. Increase up to 5 percent – 30.5%
d. Stay about the same – 53.6%
e. Decrease up to 5 percent – 10.3%
f. Decrease 5 to 10 percent – 1.6%
g. Decrease more than 10 percent – 0.6%

Average expected increase in prices consistent with these responses = 0.6%

6. Over the next year, what are your company's capital investment plans?

a. Increase more than 10 percent – 8.7%
b. Increase 5 to 10 percent – 11.8%
c. Increase up to 5 percent – 15.2%
d. Stay about the same – 40.4%
e. Decrease up to 5 percent – 9.6%
f. Decrease 5 to 10 percent – 4.7%
g. Decrease more than 10 percent – 9.6%

Average expected increase in capital investments consistent with these responses = 0.6%

7. Over the next year, what are your inventory plans?

a. Increase more than 10 percent – 1.2%
b. Increase 5 to 10 percent – 3.4%
c. Increase up to 5 percent – 12.4%
d. Stay about the same – 46.3%
e. Decrease up to 5 percent – 24.2%
f. Decrease 5 to 10 percent – 6.2%
g. Decrease more than 10 percent – 6.2%

Average expected increase in inventories consistent with these responses = –1.0%

8. Over the next year, what do you expect in terms of full-time employment in your company?

a. Increase more than 10 percent – 1.6%
b. Increase 5 to 10 percent – 6.9%
c. Increase up to 5 percent – 21.8%
d. Stay about the same – 43.3%
e. Decrease up to 5 percent – 19.9%
f. Decrease 5 to 10 percent – 4.0%
g. Decrease more than 10 percent – 2.5%

Average expected increase in full-time employment consistent with these responses = 0.2%

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 – 1.2%
b. Increase 3 to 5 percent – 15.5%
c. Increase up to 3 percent – 59.0%
d. Stay about the same – 22.0%
e. Decrease up to 3 percent – 0.9%
f. Decrease 3 to 5 percent – 0.6%
g. Decrease more than 5 percent – 0.6%

Average expected increase in employee wages consistent with these responses = 1.5%

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 – 12.8%
b. Increase 10.0 to 14.9 percent – 22.8%
c. Increase 5.0 to 9.9 percent – 41.3%
d. Increase less than 5.0 percent – 17.2%
e. No change – 2.8%
f. Decrease less than 5.0 percent – 0.6%
g. Decrease 5.0 percent or more – none
h. Uncertain – 2.5%

Average expected increase in health insurance costs consistent with these responses = 8.3%

11. Do you think the United States is headed in the right direction, or is our country on the wrong track?

a. Right direction – 8.2%
b. Wrong track – 75.4%
c. Unsure – 16.4%

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 – 58.4%
b. Weaker global growth and slower export sales – 38.8%
c. Strengthened U.S. dollar relative to other currencies – 40.1%
d. Challenges with access to capital or other forms of financing – 5.6%
e. Unfavorable business climate (e.g., taxes, regulations) – 75.2%
f. Increased raw material costs – 20.5%
g. Rising health care/insurance costs – 74.5%
h. Attracting and retaining a quality workforce – 51.6%

13. What is your company's primary industrial classification?

a. Chemicals – 6.5%
b. Computer and electronic products – 2.2%
c. Electrical equipment and appliances – 7.2%
d. Fabricated metal products – 27.1%

e. Food manufacturing – 0.6%
f. Furniture and related products – 0.3%
g. Machinery – 12.1%
h. Nonmetallic mineral products – 4.4%
i. Paper and paper products – 1.9%
j. Petroleum and coal products – 1.9%
k. Plastics and rubber products – 8.4%
l. Primary metals – 4.7%
m. Transportation equipment – 5.0%
n. Wood products – 1.6%
o. Other – 16.2%

14. What is your firm size (e.g., the parent company, not your establishment)?

a. Fewer than 50 employees – 20.5%
b. 50 to 499 employees – 54.0%
c. 500 or more employees – 25.5%

Special Questions

Regulatory Burdens

15. How has your company's total spending on state and federal regulatory compliance changed over the past few years?

a. Decreased substantially – 0.6%
b. Decreased modestly – 1.3%
c. Not changed – 15.4%
d. Increased modestly – 51.1%
e. Increased substantially – 31.5%

16. Approximately what percentage of your total current expenditures does your company devote to state and federal regulatory compliance?

a. Zero – 1.6%
b. Up to 3 percent – 29.8%
c. 3 to 5 percent – 19.6%
d. 5 to 8 percent – 12.5%
e. 8 to 10 percent – 5.1%
f. 10 to 12 percent – 3.5%
g. 12 to 15 percent – 2.6%
h. Unknown – 25.3%

Average percent of total current expenditures devoted to state and federal regulatory compliance consistent with these responses = 4.3%

17. If the cost 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 investments and expenditures – 55.8%
b. Human capital (e.g., hiring, training) – 45.2%
c. Growth and acquisition – 32.4%
d. Research and development – 36.5%
e. Debt reduction and/or increasing the return on investments – 25.3%
f. Unknown – 9.3%

Health Insurance

18. Does your company provide health benefits to your employees?

a. Yes – 98.1%
b. No – 1.6%
c. Uncertain – 0.3%

Tax Reform

The NAM has long called for comprehensive business tax reform that lowers corporate tax rates to 25 percent or less, includes a robust capital cost-recovery system and a permanent R&D incentive, moves to a modern international tax system and includes lower tax rates for “pass-through” manufacturers. As the tax debate moves forward, there is growing interest in comprehensive business tax reform that includes lower tax rates for corporate and business income earned by “pass-through” entities. The individual tax code would remain essentially the same.

19. Is your business organized as a “pass-through” entity (e.g., a subchapter S corporation, a partnership)?

a. Yes – 51.8%
b. No – 42.8%
c. Unknown – 5.5%

20. If yes, would you support comprehensive business tax reform that includes lower tax rates for corporate and business income earned by “pass-through” entities while maintaining the current individual tax code?

a. Yes – 76.8%
b. No – 4.7%
c. Unknown – 18.5%

21. Would your business be more competitive if the following policies were enacted as part of tax reform? (Check all that apply.)

a. Corporate tax rate of 25 percent or less – 74.3%
b. Competitive international tax system – 40.1%
c. Robust capital cost-recovery provisions – 55.0%
d. Permanent and enhanced R&D incentive – 61.2%
e. Permanent lower rates for “pass-through” business income – 48.5%
f. Unknown – 7.5%