Opening statement to the Senate Select Committee on Cost of Living – Manufacturing

Friday 13 September, 2024

Good morning Chair and members of the committee. My name is **Jeffrey Wilson**, Director of Research and Economics at the Australian Industry Group.

Ai Group is the peak national employer organisation representing traditional, innovative and emerging industry sectors. Our membership and affiliates include private sector employers large and small, comprising 60,000 businesses which employ over 1 million staff.

Ai Group has a particular focus on the manufacturing industry, and in 2023 celebrated our 150^{th} year supporting Australian manufacturers. We are grateful for the opportunity to appear before this hearing.

Manufacturing is a critical contributor to Australia's industrial ecosystem, and economy more broadly. There are 90,000 manufacturing businesses in Australia, which employ around 900,000 workers. It is the sixth largest industry in Australia, and produced $124 billion worth of value-add last financial year.

Manufacturing plays a key role in positively contributing to cost-of-living issues during the recent period of high inflation in Australia. Our manufacturers directly make the goods used by Australian households (food, beverages and consumer durables), and indirectly contribute by producing the industrial inputs used across the economy. Manufacturing is also highly-trade exposed, and faces stiff competition from global industrial giants in both our local and export markets.

An informed discussion of the role of industry in cost-of-living issues must start from the recognition that inflationary pressures affect both business and households alike.

The dramatic increase in consumer prices over the last three years has increased financial stress on many households. The CPI indicator has risen by 16.8% over this three-year period. But so too have producer prices – the goods and services used and made by industry – risen by a similar magnitude. Indeed, producer prices are currently rising at the rate of 4.8% per annum, faster than the 3.8% rate for CPI.

High inflation poses both cost-of-living pressures and cost-of-doing-business pressures. It is a pernicious dynamic afflicting both industry and households.

If we look at the recent performance of the manufacturing industry, it is clear that surging costs have imposed a very heavy burden.

According to official ABS price surveys, the inputs used by manufacturing have increased by 20% in price over the last three years. Some of the inputs which have seen the most dramatic increases include:

- Ferrous metals products (i.e. steel), up by 35%
- Electrical equipment, up by 40%
- Non-ferrous metals (including aluminium), up by 49%
- Basic chemicals, up by 51%
- And natural gas – the energy source which underpins much of Australian manufacturing – up by a massive 58%

Never before have our manufacturers had to contend with such a dramatic and sustained rise in prices rises for material inputs.

So too have employment pressures weighed on the industry. Over the three-year inflationary period, average wage rates in manufacturing have risen by 11.5%. This is the highest increase of any industry in Australia.

Very high increases in minimum wages in 2022 and 2023 by the Fair Work Commission played a role in this. Recent legislative changes to the industrial relations system have also introduced rigidities making life harder for manufacturing employers.

Australia's historically tight labour market posed further challenges. There are presently 17,000 unfilled jobs in manufacturing, up from 11,000 just before the pandemic. An excess of empty jobs means chronic continuity problems on the shop floor, compounding cost pressures.

Recruitment difficulties also bedevil the industry. In the June quarter of this year, 63% of recruiting manufacturers reported difficulties in filling advertised roles. This is the highest recruitment difficulty rate of any industry, and exceeds that reported by constructors, an industry with widely known hiring challenges.

These supply chain and employment pressures have led to a squeeze on manufacturer margins. Manufacturing is highly exposed to competition from imports, and often cannot fully pass on rising costs. This leaves many manufacturers more exposed to cost pressures than most other branches of industry.

In 2022-23 financial year – the most recent for which sub-industry figures are available – operating margins in Australian manufacturing fell from 8.8% to 7.9%, with nine of thirteen subindustries reporting declines. The three manufacturing subindustries that are directly oriented to consumer markets – food, beverages and TCFs – all saw significant margin declines.

This data confirms that manufacturers are feeling the pinch of inflation in the same way as consumers.

Given these factors, the recent performance of the manufacturing industry has been very weak. Manufacturing output grew by an anaemic 0.2% in real terms in the last financial year, with food manufacturing the only major branch to show meaningful growth. Employment has also fallen, with the industry shedding 12,000 jobs – 1.3% of the total – in the year to the June quarter.

Overall, this reveals the heavy burden which inflation is having on the health of Australian manufacturing. Costs have soared, labour market pressures are intense, and margins are under strain. In the face of these pressures growth has stalled, and jobs are already beginning to be shed.

These cost of doing business problems only make our cost of living challenges worse. Given the central role that manufacturing plays in our industrial ecosystem, and in producing the goods needed by Australian households, there is a pressing need to address the supply constraints across our economy that are at the root of our inflationary troubles.

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