U.S. Industrial Manufacturers Expect 2012 Growth

Barry Misthal, global industrial manufacturing leader, PwC

U.S. industrial manufacturers [1] expect continued domestic and international growth in 2012, although forecasts have fallen below 2011 actual growth rates, according to the findings of the Q4 2011 Manufacturing Barometer [2] released by PwC US [3]. While uncertainty still prevails and own-company revenue expectations have moderated, optimism about the worldwide economy rose in the fourth quarter of 2011, including a notable improvement in sentiment regarding prospects for the U.S., as compared to an all-time low in domestic sentiment in the third quarter of 2011. In addition, U.S. industrial manufacturers continue to forecast increased investment spending in the year ahead, including major outlays in operational spending. Plans for merger and acquisition (M&A) [4] activity also increased, and there was significant emphasis on expansion into new markets.

Optimism regarding the prospects of the U.S. economy over the next 12 months rose to 30 percent in the fourth quarter of 2011—up from only 5 percent in the third quarter of 2011—and 28 percent of respondents believe that the U.S. economy grew in 4Q 2011, up 21 points from the prior quarter. However, the majority of respondents, 57 percent, remain uncertain, rather than outright pessimistic. Among U.S. industrial companies operating abroad, uncertainty also remains high at 64 percent, with 36 percent believing that the world economy is declining and 48 percent reporting that they saw no change. However, 16 percent of respondents marketing abroad view the world economy as growing in the fourth quarter of 2011, up 9 points from the prior quarter.

“While forecasts remain guarded with growth rates trailing prior year actual performance, optimism about the worldwide economy increased among U.S. industrial manufacturers in the fourth quarter of 2011," said Barry Misthal, global industrial manufacturing leader for PwC [5]. “Despite the improved sentiment, however, the majority of U.S. industrial manufacturers remain cautious regarding the outlook ahead. Expectations for moderate growth in 2012 appear to be balanced by healthy cash levels, improving gross margins, and continued strategic investment spending among the major industrial manufacturers. Management teams continue to seek avenues to expand globally and gain market share, while carefully managing their risk exposure.”

Although the projected average growth rate for own-company revenue for 2012 was lowered from 5.0 percent in the prior quarter to 4.4 percent in the fourth quarter of 2011, 83 percent of respondents expect positive revenue growth for their own companies in the year ahead, while 7 percent expect growth to be negative and 10 percent expect no growth. With regard to the international contribution, industrial manufacturers continue to expect international sales [6] to deliver 38 percent of total company revenue in 2012, the same as the prior quarter and one year ago.

“While optimism about the international economy remains well below sentiment recorded in last year’s fourth quarter, expected sales contributions from overseas operations remain identical with prior year levels,” added Misthal. “At the same time, plans for spending and M&A activity continue to be a major international focus over the next 12 months. Given ongoing issues facing Asia and Europe, these findings may point to a stabilization of sentiment regarding the global outlook.”

Looking back at full year 2011, the composite average growth estimate for own-company calendar year revenue growth was 5.3 percent, down slightly from 5.6 percent projected in the third quarter survey. Eighty-seven percent of respondents said they had positive own-company growth in 2011, with 19 percent forecasting double digit gains and 68 percent projecting single digit gains. Eight percent were negative, while only 5 percent had zero growth.

Over the next 12 months, 67 percent of industrial manufacturing panelists plan major new capital investments, up 12 points from the third quarter of 2011. The level represents the highest in the past five quarters, with two out of three U.S. industrial manufacturers planning spending. However, the average level of new investment spending is expected to be lower at 4.2 percent of sales, in comparison to 5.9 percent in the third quarter of 2011. Ninety percent of respondents plan to increase operational spending, an increase of 5 points from the previous quarter. Increased operational spending is cited for new product or service introductions (57 percent), information technology (50 percent), and business acquisitions (40 percent). Forecasts for research and development spending declined 8 points to 40 percent in the third quarter of 2011, while spending forecasts pertaining to sales promotions and advertising remained low.

On the M&A front, 38 percent of industrial manufacturers say they planned activity, with virtually all of them seeking to pursue acquisitions. Forty percent plan for

expansion into new markets abroad, and 40 percent plan new joint ventures. The number planning strategic alliances rose to 35 percent, and new facilities abroad increased to 32 percent.

"The increase in planned operational spending, as well as M&A activities reflects an ongoing focus among U.S. industrial manufacturers in investing for growth in the face of an uncertain global outlook," added Misthal. "In addition, industrial manufacturing companies have continued to build liquidity, while taking steps to improve margins and provide ample support for investment in growth initiatives with a global focus."

During the fourth quarter of 2011, 38 percent of respondents reported higher gross margins, while only 15 percent said they were lower, for a net gain of 23 percent. These results are up 15 points from the third quarter of 2011, despite a continued high level of costs. In fact, 32 percent of U.S.-based industrial manufacturers reported higher costs, while 15 percent reported cost reductions, for a net plus of 17 percent, 11 points below the third quarter. In addition, 30 percent raised prices, but 8 percent lowered them, for a net plus 22 percent reporting higher prices, up 12 points from the third quarter.

Looking at the employment picture, 37 percent of respondents plan to add employees to their workforces [7] over the next 12 months, off 1 point from the third quarter of 2011. However, the net workforce composite projection rose from a minus 0.2 percent in the prior quarter to a plus 0.7 percent, representing modest gains and a break from what had been a declining hiring pattern in past surveys. Among those respondents planning to hire, the most sought after employees will be professionals and technicians (28 percent), and skilled workers (23 percent). Interest in production workers declined to 13 percent, off 14 points from the third quarter of 2011.

Regarding expected barriers to business growth, legislative and regulatory pressures were cited most by respondents at 50 percent. Lack of demand and oil/energy prices were next at 47 percent, with both being down from the previous quarter. Taxation concerns dropped 7 points to 33 percent, while concerns about decreasing profitability fell sharply to 18 percent.

"The success of U.S. industrial manufacturers in increasing operating profitability remains a major bright spot in the prolonged challenging global marketplace," added Misthal. "In the fourth quarter PwC Manufacturing Barometer, concerns about profitability holding back growth were the lowest in over 12 months, highlighting the fundamental strength of U.S. manufacturers in spite of ongoing sales pressures and intense global competition."

Special Topic: Supply Chain And Global Operations

U.S. industrial manufacturers continue to focus on improving company supply chains [8] globally. According to the fourth quarter PwC Manufacturing Barometer, three quarters (77 percent) of industrial manufacturers surveyed believe it is very or extremely important to the growth of their global businesses to improve their companies' supply chain over the next two to three years.

Forty three percent of respondents confirmed it is very/extremely important to improve their companies' globalized product development operations, while 40 percent sited their supply base and 39 percent sited their manufacturing footprint as major priorities. In addition, 75 percent of respondents confirmed definite plans for major/minor improvement of their globalized distribution systems over the next 12 to 18 months.

Moreover, 78 percent of industrial manufacturers surveyed believe their current business is scalable to meet global requirements at target performance levels over the next two to three years—50 percent definitely and 28 percent probably. The majority (52 percent) of respondents envision the need to rethink and/or reprioritize their companies' manufacturing core competences to grow and optimize their business during the next two to three years. Overall, 57 percent of industrial manufacturers see a need to partner in new ways with their strategic suppliers to grow and optimize their business over the next two to three years.

About the Manufacturing Barometer
PwC's Manufacturing Barometer [2] is a quarterly survey based on interviews with 60 senior executives of large, multinational U.S. industrial manufacturing companies about their current business performance, the state of the economy, and their expectations for growth over the next 12 months. This survey summarizes the results for Q4 2011 and was conducted from October 26 through January 11, 2012.

To view the complete Manufacturing Barometer report, visit http://www.pwc.com/manufacturing-barometer [2]. For information about other Barometer surveys, including recent economic trend data and topical issues, visit http://www.barometersurveys.com [9].

About PwC's Industrial Manufacturing Practice
PwC's Industrial Manufacturing practice *[1] comprises a global network of industry professionals strategically located in more than 30 countries around the world. The practice brings experience, international industry best practices, and a wealth of specialized resources to help solve business issues.*

About PwC's Industrial Products Practice
PwC's Industrial Products *[10] (IP) practice provides financial, operational, and strategic services to global organizations across the* aerospace & defense *[11] (A&D),* business services *[12],* chemicals *[13],* engineering & construction *[14] (E&C),* forest, paper, & packaging *[15] (FPP),* industrial manufacturing *[1],* metals *[16], and* transportation & logistics *[17] (T&L) industries. With more than 31,000 professionals located in over 150 countries, PwC's IP global professionals deliver a wide range of industry-focused tax, assurance, and advisory services to address critical business issues. For more information, please visit* www.pwc.com/us/en/industrial-products *[18]*

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