

MARKET SECTOR INSIGHTS - FEBRUARY 2019

Manufacturing Industry



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Global Outlook

According to a report by the United Nations Industrial Development Organization (“UNIDO”), the rate of global manufacturing growth slowed down in 2018 primarily as a consequence of trade and tariff barriers in many countries around the globe. Going into the details, the report adds that world manufacturing value added rose by 3.6% in 2018, slightly lower than the 3.8% recorded in the previous year. This slowdown can be mainly attributed to emerging trade and tariff barriers involving the US and China, as well as the US and the European Union (“EU”), which have exposed markets to a significant amount of uncertainty. This limits investment and future growth as China, the EU and the US account for over half of global manufacturing production.

This slowdown in manufacturing in 2018 was observed in both industrialised economies as well as developing and emerging industrial economies. The manufacturing value added (“MVA”) growth rate for industrialised countries rose by 2.3% in 2018, compared to 2.6% in 2017, whereas for the group of developing and emerging industrial economies, the MVA growth rate in 2018 was 3.8%, down from 4.1% in 2017. In North America, manufacturing production maintained comparatively higher growth, mainly due to increased growth rates in the US where manufacturing production rose at the higher pace of 3.1% in 2018, compared to 1.8% in 2017. However, in the EU and East Asian countries, the annual manufacturing growth rate decreased, from 3.5% to 2.6%, and from 3.1% to 1.9%, respectively.

Going forward, the global manufacturing industry is expected to witness steady growth propelled by healthy annual growth rates in the US and Asia; however, challenges remain such as increasing protectionism as well as declining consumer demand in some countries in Europe and North America.



Challenges in the Manufacturing Industry

- **Labour shortage:** Manufacturers across industrialised nations are finding it difficult to fill positions, both skilled and unskilled. Reasons for this range from lack of robust training programs to manufacturers in many places not being able to attract workers.
- **Keeping up with new technologies:** Technology is advancing very rapidly, and most manufacturers today are struggling to keep up, let alone stay ahead of competition.
- **Global competition:** Many of the formerly developed industrialised nations are facing stiff competition from countries such as China and India owing to the availability of plentiful and cheap resources in these countries.
- **Cybersecurity:** As technology advances, so do the efforts and skills of cybercriminals. While ransomware was once the most common form of cybercrime, after years of rampant growth it's been overtaken by two “new” threats: banking trojans and cryptominers. However, the majority of manufacturers are relying on outdated security systems incapable of addressing the number and complexity of threats today, leaving many of them prone to costly security breaches

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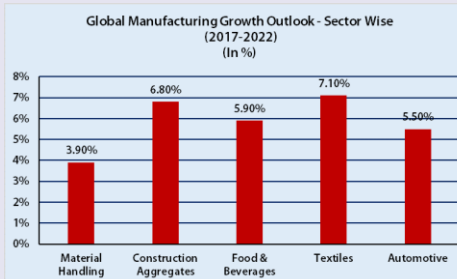


Figure 7. Global manufacturing outlook by sector, 2017-2022.



Sector Growth

Construction aggregates and textiles are expected to be the fastest growing sectors in manufacturing in the coming years, with both expected to witness growth at a CAGR of around 7% between 2017-2022. The next fastest growing sectors are automotive and food processing, with projected growth at a CAGR of around 6% between 2017-2022. In terms of machineries, material handling equipment manufacturing is the largest sector and is expected to grow at a CAGR of 3.9% between 2017-2022.



Impact of Automation on Manufacturing

The fact that automation is steadily changing the manufacturing industry cannot be denied. Over the past few years, the industry has seen innumerable advancements in automation and its implementation in manufacturing cycles across the globe. Be it labour shortage solutions, increased worker safety, reduced occurrence of human error, reduced employee costs or increased production, automation has had and is having a significant impact on manufacturing in all sectors.

The thought that existed widely until some years ago and still exists in some quarters about automation taking away the bulk of jobs and leaving people jobless might have led to uneasiness about its implementation in the past, but based on empirical evidence, it has become clear that automation will not result in significant job loss. In fact, it might open up new avenues for job seekers. Going forward, experts expect much wider usage of automation technology in the manufacturing industry.



US Outpacing China

China might have been the largest manufacturing nation in the world until some years ago, but lately it's been the United States where manufacturing is rapidly growing. According to Deloitte's Global Manufacturing Competitive Index ("GMCI"), the US will outpace China as the world's most competitive manufacturing nation by 2020.

This change primarily comes down to an ongoing economic boom that some analysts are calling "Manufacturing 4.0" or "Next Manufacturing." Manufacturers in the US today are finding that the total cost of ownership ("TCO") favours US-based factory production. Plus, the domestic energy boom in natural gas and fracking has lowered the cost of materials and operations, prompting more factories to return to US soil. US-based plants benefit from the proximity to a growing field of local raw materials suppliers. Keeping production in the country means there are no duties or tariffs and inventory carrying costs are reduced. Additionally, R&D innovations on the factory floor aren't at risk of intellectual property theft.



UK Manufacturing

According to a January 2019 article from Bloomberg, UK manufacturers are more pessimistic than at any time since the Brexit referendum. According to a survey from the Confederation of British Industry ("CBI"), the manufacturing lobby group's index of confidence slumped to minus 23 in January 2019, the weakest level since the aftermath of the 2016 vote to leave the European

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Union. Moreover, export prospects hit their lowest level since the financial crisis and firms plan to spend less on investment than they did in 2018. CBI stated, "Notably, the number of firms citing political/economic conditions abroad as a factor likely to limit export orders in the next three months was at its highest since July 2016."

The article stated, "The bleak outlook comes amidst heightened fears that Britain is heading out of the EU without a deal and days after the International Monetary Fund downgraded its global outlook. Demand is softening in Europe, the biggest market for UK exports, and the giant Chinese economy grew at its slowest pace since 2009 last quarter."

Similarly, in March 2019 the Financial Times reported that UK manufacturing outlook is the dimmest since 2012, and things aren't expected to improve, with seemingly no end in sight to the impasse over Brexit.

Recent Trends



Emergence of IoT

Manufacturers are increasingly leveraging the Internet of Things ("IoT"), which is comprised of the interconnection of unique devices within an existing Internet infrastructure to achieve a variety of goals including cost reduction, increased efficiency, improved safety, meeting compliance requirements and product innovation.

The IoT's existence can be primarily attributed to three factors: widely available Internet access, smaller sensors and cloud computing. In a recent survey, roughly 63% of manufacturers believe that applying IoT to products will increase profitability over the next five years and thus have planned to invest a combined total of \$267 billion in IoT by 2020. These are the manufacturers who understand that IoT empowers them to make informed strategic decisions by providing crucial, real-time information. The IoT is having a major impact on manufacturing, primarily by opening up the possibility of connecting operations and transforming business processes.



Emphasis on Supply Chain

One of the most notable recent trends in the global manufacturing industry is the move from the traditional model for supply chains to creating a digital supply network for manufacturing. An intelligent and connected supply chain is quickly becoming the foundation that manufacturers can use to work more collaboratively with suppliers and customers to boost business efficiency and deliver improved product and service innovation.

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Manufacturers are increasingly coming around to believe that creating an effective enterprise supply chain network is an important part of fully realizing the potential of manufacturing. Industry experts expect more innovations in this sphere in the next few years, which will benefit both manufacturers and consumers.



Focus on B2B2C

Manufacturers who had a conventional B2B ("Business-to-Business") business model are increasingly focusing on the B2B2C ("Business-to-Business-to-Consumer") model due to the numerous benefits provided by selling products directly to end consumers.

Some of the notable benefits of this model are: manufacturers receiving the full MSRP ("Manufacturer's Suggested Retail Price") on products rather than wholesale prices which is currently the norm; and manufacturers getting the opportunity to test and consequently market products quickly, which opens up the possibility of manufacturers getting the first mover advantage in many cases. Other benefits of this model include price control and eliminating the possibility of brand misrepresentation.



European Valuations' View

The manufacturing industry contributes a large share to any country's GDP and also to the global GDP along with giving employment to millions across the globe. However, the importance of manufacturing industry also makes it vulnerable to external factors such as protectionism, declining consumer sentiment, geopolitical events and many more. In the long term, steady global economic growth powered by countries such as China, India and in part the US and Europe, will spur manufacturing activity, but in the short term, manufacturers should remain cautious as the aforementioned external factors are likely to have an impact leading to a possible downturn in global manufacturing. To stay ahead of the competition today, manufacturers should focus on greater integration of technology into their processes, accepting and planning for changing consumer behaviour and using innovation to drive their business forward.

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