

Manufacturing recovery sustained in May, but new order growth slows

Key findings:

- Sharpest increase in production volumes since June 2015
- New order growth loses momentum amid slight fall in export sales
- Rate of job creation moderates from 16-month high recorded in April

Canadian manufacturers experienced another modest upturn in overall business conditions during May, which marked three months of sustained improvement. Output growth expanded at its fastest pace for almost one year, but the latest survey pointed to slightly weaker rates of new business and employment growth. There were also signs of pressure on operating margins as input cost inflation accelerated in May, while output charges were broadly unchanged.

The headline figure derived from the survey is the RBC Canadian Manufacturing *Purchasing Managers' Index*™ (PMI™), which is designed to provide timely indications of changes in prevailing business conditions in the Canadian manufacturing sector. PMI readings above 50.0 signal an improvement in business conditions, while readings below 50.0 signal deterioration.

At 52.1 in May, the seasonally adjusted RBC Canadian Manufacturing PMI was above the neutral 50.0 mark and only fractionally lower than the 16-month high of 52.2 recorded in April. As a result, the headline index indicated another moderate improvement in business conditions across the manufacturing sector, mainly supported by greater levels of output, new business and employment in May. Moreover, the average PMI reading so far this quarter indicates the strongest growth momentum since Q4 2014.

May data signalled a solid expansion of production volumes, with the latest rise the fastest since June 2015. Survey respondents noted that greater new business volumes and improved confidence regarding the general economic outlook had underpinned the increase in output levels. New order volumes picked up for the

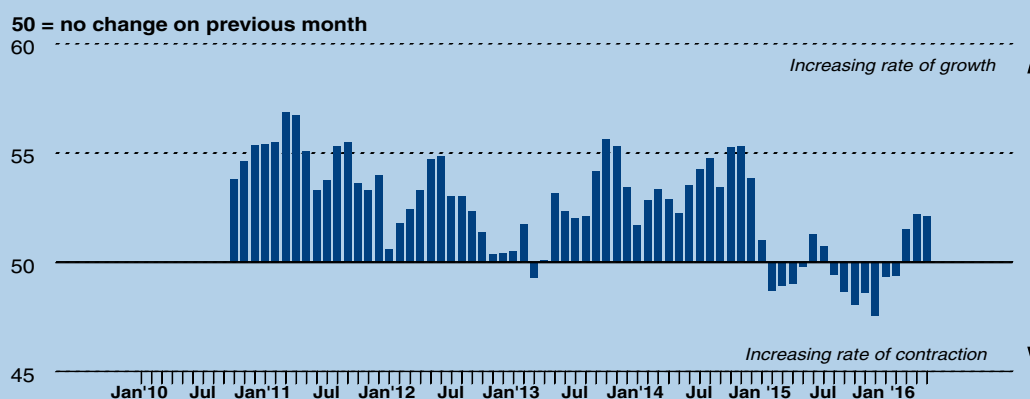
third month running in May, which mirrored the trend recorded for production volumes across the manufacturing sector. However, the latest survey signalled a slight loss of momentum from the 16-month high seen during April.

Anecdotal evidence suggested that new product launches and gradually improving demand conditions had supported manufacturing sales, while subdued investment spending and cautious inventory management among clients remained key growth headwinds. Export sales were also a drag on overall new business intakes across the manufacturing sector in May. Although only marginal, the reduction in new work from abroad was the first since October 2015.

Manufacturing firms boosted their staffing levels in May, as has now been the case for the past three months. Another increase in staff recruitment helped to drive a modest reduction in work-in-hand (but not completed) across the manufacturing sector, thereby extending the current period of backlog depletion to 18 months running.

The latest survey pointed to cautious inventory policies at manufacturing firms in May. Stocks of finished goods declined at the fastest pace since January, while pre-production inventories fell despite higher volumes of input buying. Moreover, lead times from vendors lengthened amid reports of capacity cuts and reduced stocks among suppliers. Meanwhile, input cost inflation accelerated over the month, which survey respondents mainly linked to higher steel prices and the weak exchange rate. Factory gate charges were nonetheless broadly unchanged in May, which firms linked to weak pricing power and intense competitive pressure.

RBC Canadian *Purchasing Managers' Index*™ (PMI™)



Components of the RBC Canadian Manufacturing PMI™

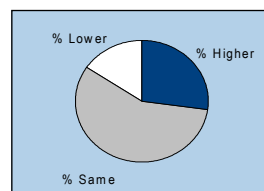
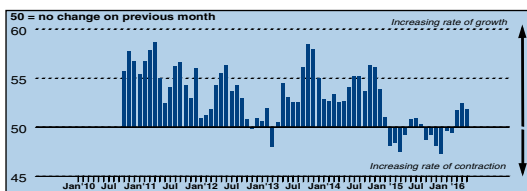
The RBC Canadian Manufacturing *Purchasing Managers' Index*™ (PMI™) is a composite index designed to show a convenient single-figure summary of the health of the manufacturing sector. The five individual indices used in the headline PMI and their weightings are:

New Orders	0.30
Output	0.25
Employment	0.20
Suppliers' Delivery Times (inverted)	0.15
Stocks of Purchases	0.10

In total, the RBC Canadian Manufacturing PMI survey covers eleven individual indicators that are presented as 'diffusion' indices. These are summary measures showing the prevailing direction of change. An index reading above 50.0 indicates an overall increase in that variable, whilst index readings below 50.0 signal an overall decrease. All data are seasonally adjusted.

New Orders Index (0.30)

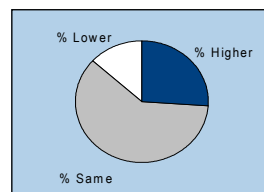
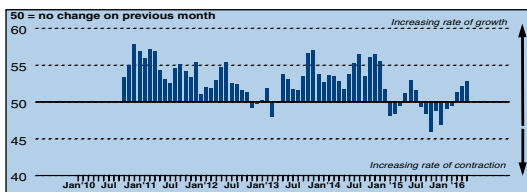
Q. Please compare the state of your new orders (in units) this month with one month ago.



Manufacturers indicated an uptick in new business volumes for the third month running in May, but the pace of expansion eased slightly since April and remained modest overall. Survey respondents suggested that new product launches and improving underlying demand had boosted sales at their plants. However, some firms commented on weak demand for capital goods and cautious inventory policies among clients.

Output Index (0.25)

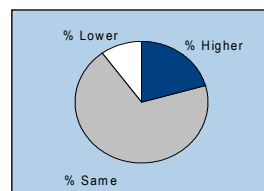
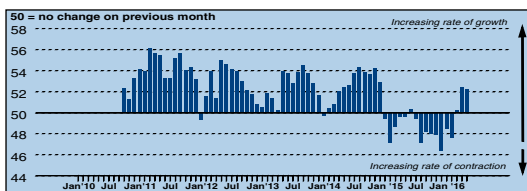
Q. Please compare your production/output this month with the situation one month ago.



The seasonally adjusted Output Index registered above the 50.0 no-change threshold in May, which extended the current period of sustained production growth to three months. Moreover, the latest reading signalled the fastest increase in output volumes since June 2015. Manufacturers mainly cited greater new business volumes and improved confidence regarding the general economic outlook.

Employment Index (0.20)

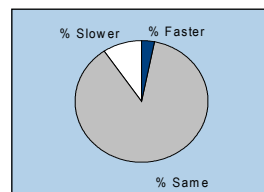
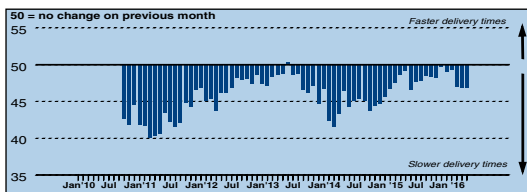
Q. Please compare the level of employment at your unit this month with the situation one month ago.



May data highlighted additional staff hiring across the manufacturing sector. Although the pace of job creation was only moderate, the seasonally adjusted Employment Index remained close to its highest level recorded over the past year-and-a-half. A number of firms noted that greater workloads in recent months had encouraged them to boost their payroll numbers.

Suppliers' Delivery Times Index (0.15)

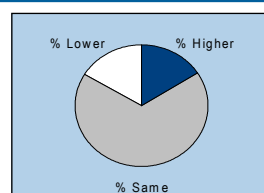
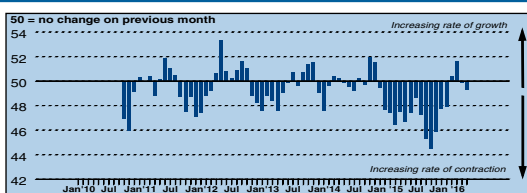
Q. Please compare your suppliers' delivery times (volume weighted) this month with one month ago.



Adjusted for seasonal influences, the Suppliers' Delivery Times Index posted below the neutral 50.0 value for the thirty-fifth consecutive month in May, thereby signalling a further lengthening of average lead times from vendors. Anecdotal evidence suggested that low stocks and capacity cutbacks had led to supply chain bottlenecks in the wake of rising demand for raw materials in recent months.

Stocks of Purchases Index (0.10)

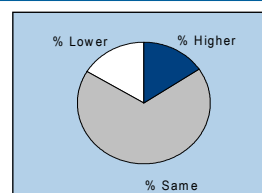
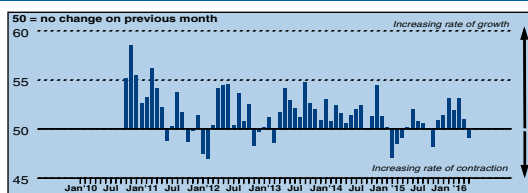
Q. Please compare your stocks of purchases (in units) this month with the situation one month ago.



Pre-production inventories were depleted for the second month in a row during May. The seasonally adjusted Stocks of Purchases Index eased to its lowest since January, but signalled only a marginal rate of decline. Some manufacturers reported that longer than expected lead times for raw materials, alongside generally rising client demand, had contributed to reduced stocks of purchases at their plants.

New Export Orders Index

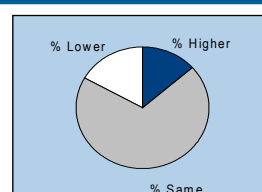
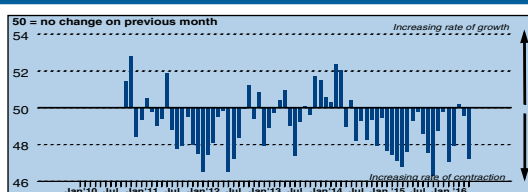
Q. Please compare the state of your new export orders (in units) this month with one month ago.



Canadian manufacturers indicated a return to falling new export orders in May, which ended a six-month period of sustained expansion. Although panel members noted that the weak exchange rate remained supportive of new sales wins from abroad, some firms commented on subdued underlying demand from export clients (particularly outside of the US).

Stocks of Finished Goods Index

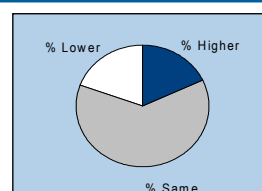
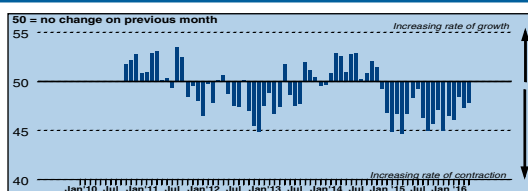
Q. Please compare your stocks of finished goods (in units) this month with the situation one month ago.



Post-production inventories decreased for the second month running in May. Adjusted for seasonal influences, the Stocks of Finished Goods Index pointed to a solid pace of decline that was the fastest since January. There were reports that lower stocks of finished goods reflected greater than expected sales. However, some firms commented on deliberate inventory reduction in order to boost cash flow.

Backlogs of Work Index

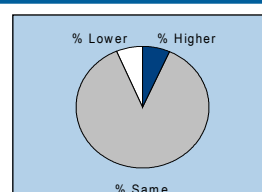
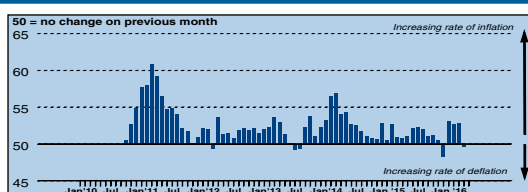
Q. Please compare the level of outstanding business in your company this month with one month ago.



May data suggested a continued lack of pressure on operating capacity across the manufacturing sector. This was highlighted by a sustained reduction in unfinished work at manufacturing companies in May, with the seasonally adjusted Backlogs of Work Index posting below the neutral 50.0 threshold for the eighteenth month running.

Output Prices Index

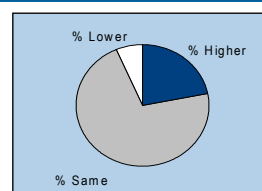
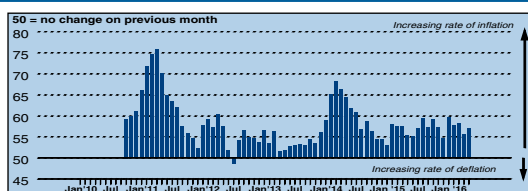
Q. Please compare the average price that you charge per unit of output (volume weighted) this month with one month ago.



Average prices charged by Canadian manufacturers were virtually unchanged in May, as highlighted by the seasonally adjusted Output Prices Index registering broadly in line with the 50.0 no-change threshold. Reports from survey respondents suggested that subdued pricing power had persisted in May, which meant that operating margins remained under pressure from higher input costs.

Input Prices Index

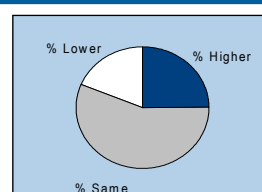
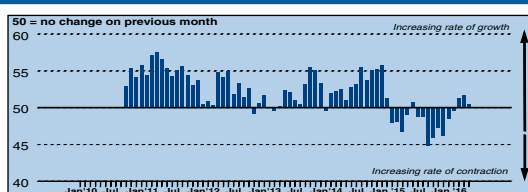
Q. Please compare the average price of your purchases (volume weighted) this month with the situation with one month ago.



The seasonally adjusted Input Prices Index signalled a robust and accelerated increase in average cost burdens across the manufacturing sector in May. However, the rate of inflation was still slower than the long-run survey average. There were widespread reports of higher steel prices during the latest survey period. Panellists also noted upward pressure on imported raw material costs linked to the exchange rate.

Quantity of Purchases Index

Q. Please compare the quantity of items purchased (in units) this month with the situation one month ago.



Adjusted for seasonal influences, the Quantity of Purchases Index posted above the 50.0 no-change value for the third month running, but the latest increase in input buying was only marginal and the weakest recorded during this period. Companies that reported an upturn in input buying generally cited sustained production growth and the launch of new products.



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With nearly 8000 members working across the private and public sectors, SCMA is the principal source of supply chain training, education and professional development in the country. Through its 10 Provincial and Territorial Institutes, SCMA grants the Supply Chain Management Professional (SCMP) designation, the highest achievement in the field and the mark of strategic supply chain leadership.

SCMA was formed in 2013 through the amalgamation of the Purchasing Management Association of Canada and Supply Chain and Logistics Association of Canada. With a combined history of more than 140 years, today the association embraces all aspects of strategic supply chain management, including: purchasing/procurement, strategic sourcing, contract management, materials/inventory management, and logistics and transportation.

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The RBC Canadian Manufacturing Purchasing Managers' Index™ (PMI™), produced by Markit and in association with PMAC, is based on data compiled from monthly replies to questionnaires sent to purchasing executives in over 400 industrial companies. The panel is stratified by company workforce size and by Standard Industrial Classification (SIC) group, based on industry contribution to Canadian GDP.

Survey respondents reflect the change, if any, in the current month compared to the previous month based on data collected mid-month. For each of the indicators, the 'Report' shows the percentage reporting each response, the net difference between the number of higher/better responses and lower/worse responses, and the diffusion index. This index is the sum of the positive responses plus a half of those reporting 'the same'.

Diffusion indexes have the properties of leading indicators and are convenient summary measures showing the prevailing direction of change. An index reading above 50.0 indicates an overall increase in that variable, below 50.0 an overall decrease. All data are seasonally adjusted.

Markit do not revise underlying survey data after first publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series.

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