AUSTRALIAN INDUSTRY GROUP

Private New CAPEX – June Quarter 2010

ECONOMIC ALERT

26 AUGUST 2010

KEY POINTS

CAPEX by total and asset type

- The volume of private new capital expenditure fell by 4.0% in the June quarter 2010 (seasonally adjusted), following a (revised down) fall of 1.0% in the March quarter.
- The June quarter result was significantly worse than the median market forecast of a rise of 2.3%.
- The annual rate of change worsened, from a fall of 0.3% in the March quarter to a fall of 4.8% in the June quarter 2010.
- Investment in building and structures (volumes) fell by 3.9% in the June quarter, following a 6.4% rise in the previous quarter, to be 7.2% lower over the year.
- Investment in equipment, plant & machinery fell solidly in the June quarter 2010, down 4.1%, following a 7.2% fall in the previous quarter. In the year to the June quarter 2010, investment in equipment, plant & machinery fell by 2.4%.

CAPEX by industry

- Manufacturing capital investment rose by 16.5% in volume terms in the June quarter 2010, to be 2.2% higher than a year ago.
- The seasonally adjusted volume of expenditure by the manufacturing sector on buildings & structures rose by 26.7% in the quarter, while the volume of expenditure on equipment, plant & machinery rose by 11.3%.
- Elsewhere, investment in mining rose by 2.6% in volume terms in the June quarter, following a 2.8% rise in the March quarter 2010. The volume of mining investment in the June quarter was 2.6% higher than a year ago.
- Investment in ‘other selected industries’ fell sharply by 10.9%, to be 10.2% lower than a year ago.

CAPEX expectations

- The ABS released its seventh set of investment expectations data relating to 2009-10 (that is the actual outcome for the year). In current prices, the outcome was $106,076 million. This is 6.2% lower than the seventh estimate for 2008-09, and 1.8% lower than the sixth estimate for 2009-10.
- The estimate of total investment in 2009-10 implies a fall in current price private capital investment of around 6.2% in 2009-10. This slightly worse than the 2010-11 Budget forecast of a 2.0% fall in business investment in 2009-10 in volume terms.
- For the manufacturing sector, the actual current price outcome for investment in 2009-10 ($11,705 million) is 0.6% lower than the sixth estimate for 2009-10 and represents a 7.7% fall in investment expenditure compared to 2008-09.
- The ABS also released its third estimate for total investment in 2010-11 today. This estimate is for investment of $123,334 million. Using the outcome of $106,076 million for investment in 2009-10 and a ten-year average realisation ratio of 1.10 for investment in 2010-11 implies strong growth in the value of total investment of 28% in 2010-11. This compares with a 2010-11 Budget forecast of growth of 7.0% in the volume of business investment in the same year.

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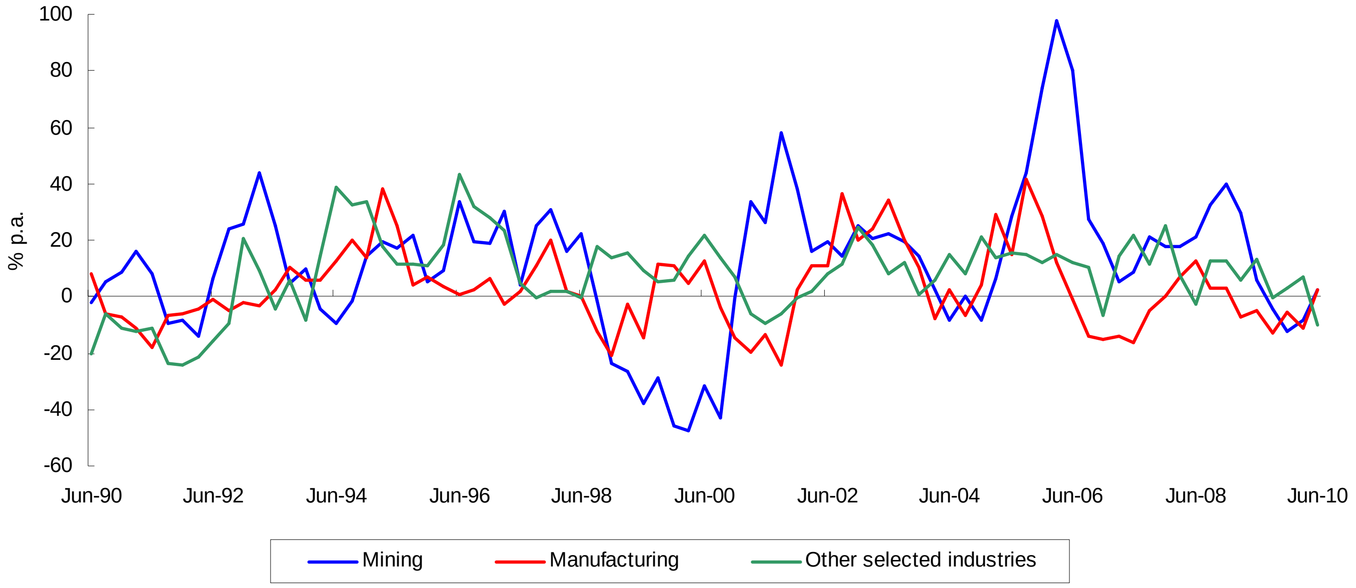
Chart: Annual growth in actual capital expenditure by major sector (chain volume measure)



Policy implications

- Today's June quarter 2010 investment data suggest that recent uncertainty around the global economy, including China, higher domestic interest rates, uncertainty on the Government's mining tax, and the high level of the Australian dollar have had an impact on short-term investment outcomes, particularly in the services sector.
- However, expectations for investment in 2010-11 have lifted and remain strong.
- Overall, taking into account reasonable realisation ratios, business investment expectations in the longer-term appear to be consistent with a sustained lift in aggregate investment in 2010-11.
- The high levels of expectation for investment in 2010-11 in particular, reflect recent still solid levels of business confidence and a number of large-scale projects, including the Gorgon LNG project and the ongoing expansion of the Pilbara iron ore mines.
- Recent softness in investment, combined with modest growth in consumer demand, suggests that the Reserve Bank Board is likely to wait and see how the economic data develops before changing the current stance of monetary policy. However, as we move into 2011, the expected lift in investment, though it will help to limit supply side capacity constraints, will help to underpin employment, and consequently wages, growth.
- The RBA Board is likely to become more vigilant on inflationary pressures towards the end of 2010 with the potential for further, modest increases in the cash rate.