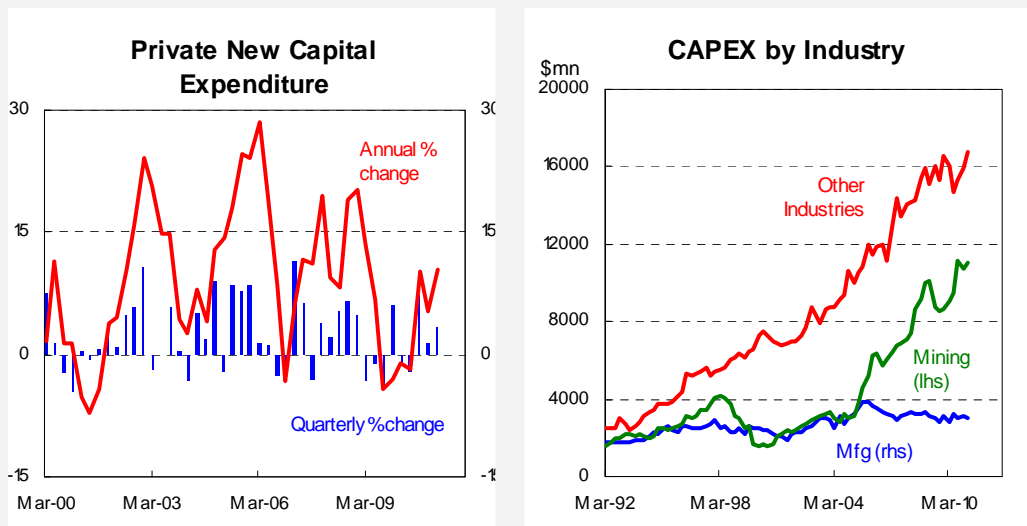


DATA SNAPSHOT

CAPEX is 'On Song'

Thursday, 26 May 2011

- Today's data underscores that the growth engine of the Aussie economy - private business investment - is properly tuned and running sweetly. Actual spending by private businesses rose by 3.4% in the March quarter, taking the annual rate to a two-year high of 10.6%.
- The intentions of businesses for spending this financial year and next year also remains very strong, especially in the mining sector. But there was a modest downgrade to overall spending plans for this financial year, which was almost offset by an upgrade for next financial year. We estimate that investment growth in 2010-11 will be 15.8% and in 2011-12 will be 43.5%.
- This upswing in business investment will continue to underpin economic activity and lower spare capacity in the economy, causing underlying inflation pressures to build. This upswing supports our view that more tightening from the Reserve Bank is on the cards.



Capex – Actual Spending:

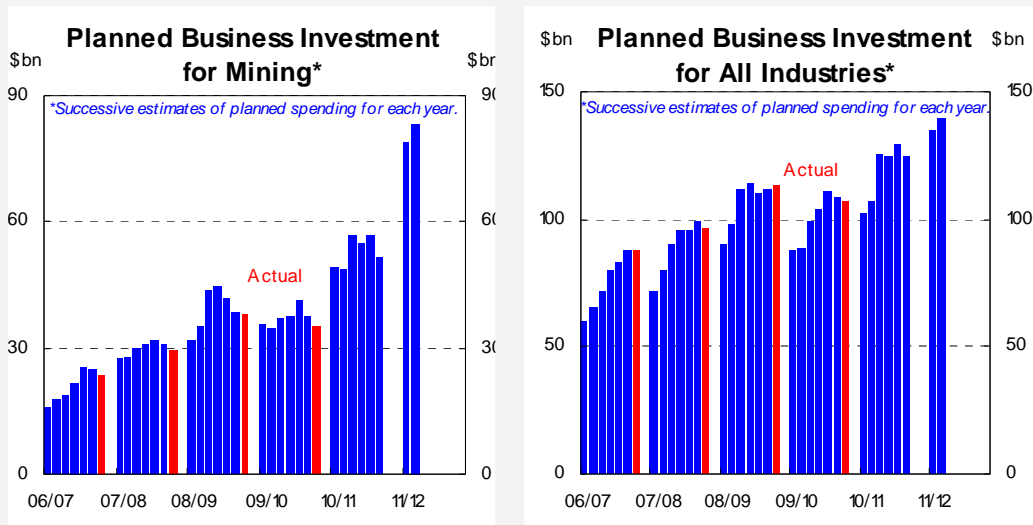
Private business investment (or capex) rose by 3.4% in the March quarter. It takes the annual rate of growth to 10.6%, the highest rate in two years.

Business investment as a share of the Australian economy (as measured by GDP) is high and reflects the attractive return to capital, particularly for resource companies.

A breakdown of the data shows that growth was broad based across the asset classes. Spending on buildings rose by 4.5% in the quarter and by 17.2% on a year ago. Spending growth on equipment, plant & machinery was 2.4% higher in the quarter and 4.2% higher on a year ago.

By industry, growth in the March quarter was mixed. Not surprisingly, spending lifted in the mining sector, by 2.8%, taking the annual growth rate to 21.3%. Business spending also lifted in other selected industries, by 5.4% in the March quarter and by 4.7% on a year ago.

Spending by businesses in the manufacturing industry, however, fell by 4.2%, although the annual growth rate is healthy at 9.1%. The high level of the Australian dollar is making it tougher for the manufacturing industry, notably traditional manufacturing.



Capex – Spending Plans:

The intentions to spend by businesses for this financial year and next year remain very strong, especially in the mining sector. But there was a modest downgrade to spending plans for this financial year (of \$5.1bn), almost offset by an upgrade next financial year (of \$4.7bn).

We received the sixth estimate for what private businesses plan to spend for 2010-11. The sixth estimate for total spending was \$124.1bn. This estimate is 14.2% higher than what the corresponding sixth estimate was for 2009-10 but is 4% lower than the 5th estimate for 2010-11.

Using the average realisation ratios over the last five years, the sixth estimate implies business investment will grow by 15.8% this financial year. That represents a slight downward revision from the previous quarter when spending intentions were \$129.2bn and growth was estimated to be 22%.

More importantly, we also received the second estimate for the next financial year of 2011-12. The second estimate for total spending in 2011-12 is \$139.5bn, which is 30.9% higher than what the second estimate was for 2010-11. It is also \$4.7bn or 3.5% higher than the first estimate for 2011-12.

Typically, there can be quite some variation between the early estimates (such as the second estimate received for 2011-12) and what the final actual result will show. However, using realisation ratios, we estimate that a very strong increase of investment is set to come through for next year. Indeed, we estimate that business investment will grow by a staggering 43.5% in 2011-12 – an upgrade from the 39.8% expected at the time of the previous survey (when spending intentions were \$134.9bn).

- By Type of Asset

For buildings & structures, the sixth estimate for 2010-11 was downgraded but the second estimate for 2011-12 was upgraded.

For plant & equipment, the sixth estimate for 2010-11 and the second estimate for 2011-12 were both upgraded.

- By Industry

Across all industries, the sixth estimate for 2010-11 was revised lower in mining and manufacturing but upgraded in other selected industries.

The second estimate for 2011-12 was higher across mining and other selected industries but lower in manufacturing when comparing with the first estimate.

Mining then was the only industry to record a downgrade for both 2010-11 and 2011-12. But even with these downgrades, we estimate business investment growth in the manufacturing sector will be 2.9% in 2010-11 and 6.7% in 2011-12. The recent WBC-ACCI survey of industrial trends also suggests investment intentions are positive for manufacturing in anticipation of reconstruction activities in Queensland.

GDP Implications:

The equipment, plant & machinery spending component from this data feeds into the GDP equation. It indicates that this segment is likely to make a positive contribution to GDP. However, the combination of the remaining components of GDP still suggest that the Aussie economy likely contracted in the March quarter. This contraction is largely to the temporary impacts from the natural disasters. GDP is expected to recover from the flood-induced contraction in the June quarter.

Cash Rate Implications:

The impact of greater business investment in the year ahead will filter through to the broader economy, underpinning economic activity. This strong business investment story will continue to cause spare capacity to fall and help drive up the underlying inflation rate. It, therefore, supports our long-held view that the Reserve Bank is likely to start raising rates. We still favour the first tightening for this year occurring in Q3 but we would not fully rule out an earlier move.

Footnote:

Each quarter, the Bureau of Statistics releases an estimate for the current financial year and/or an actual figure. It also releases an estimate or actual figure for the next financial year. There are six estimates, followed by the actual data. Thus, the charts show six blue bars (representing the estimates) and a green bar, which is the actual outcome.

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