Economics
November 25 2010

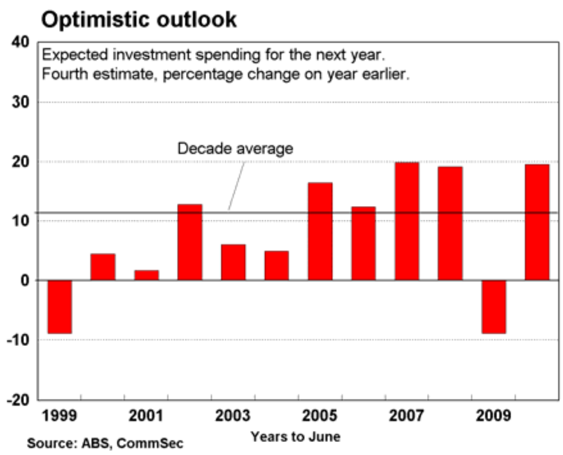
Mining investment leads the way

Private New Capital Expenditure

- **New business investment rose by 6.2 per cent in the September quarter – the biggest increase in three years. Mining dominated investment plans with investment in the sector up by 15.6 per cent as opposed to manufacturing investment which fell by 6.3 per cent in the September quarter.**
- **Equipment spending fell by 1.1 per cent in the quarter while spending on buildings rose by 13.4 per cent.**
- **Businesses expect to invest $123.9 billion in the 2010/11 year unchanged on the third estimate from the June quarter and slightly down on the usual (decade average) upgrade of 1.7 per cent made by firms at this time of the year. Investment plans are up 19.5 per cent on the equivalent estimate made a year ago.**

What does it all mean?

- At first glance the latest pick up in capital investment looks encouraging. The 6.2 per cent lift in September quarter investment marks the biggest increase in three years. However a closer look at the data highlights that the pickup in investment is far from uniform, rather it is the mining sector that is driving investment.
- In recent times the Reserve Bank has been commenting on the re-emergence of the two speed economy and the resulting structural shift in labour and investment resources. And this thematic is no more evident than in the release of the latest business investment data. Mining investment surged by almost 16 per cent in the quarter while manufacturing investment tracked sharply lower. Interesting the higher Aussie dollar is acting as a strangle hold on many industries including manufacturing, tourism and exports outside of the resources space.
- Over the coming year it is clear that Australia will be riding on the back of the mining sector. Though the non-mining states are unlikely to feel the effects of the rise in incomes until the recovery is well and truly in full swing. In fact over 80 per cent of the pickup in mining investment was focused squarely on Western Australia and Queensland. No doubt as the recovery gains traction the mining states will be in the driver's seat and continue to enjoy strong investment flows.
- As the public sector takes a step back in activity it will be up to the private sector to drive investment and growth going forward. And while the overall rise in investment over the past quarter is heartening, the estimate for future



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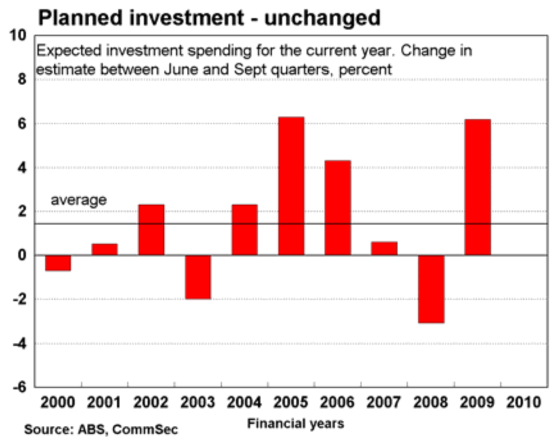
spending is a touch disappointing. Business expect to invest around $124 billion over 2010/11 a result that was unchanged on the June quarter estimate and suggests that a healthy level of caution is still part of the business landscape.

- The unchanged estimate for future spending is unlikely to concern the Reserve Bank at this stage, especially given that planned investment is still up almost 20 per cent on a year ago. What the Reserve Bank does not want to see is planned investment effectively going nowhere for a couple of quarters. A lift in investment is encouraging for the economy as a whole, serving to boost productive capacity and therefore keep any potential inflationary pressures in check.
- The latest result is unlikely to alter the Reserve Bank view that interest rates will continue to rise over the coming year. However it is likely that in the near term interest rate will remain on hold until Corporate Australia ramps up future spending.

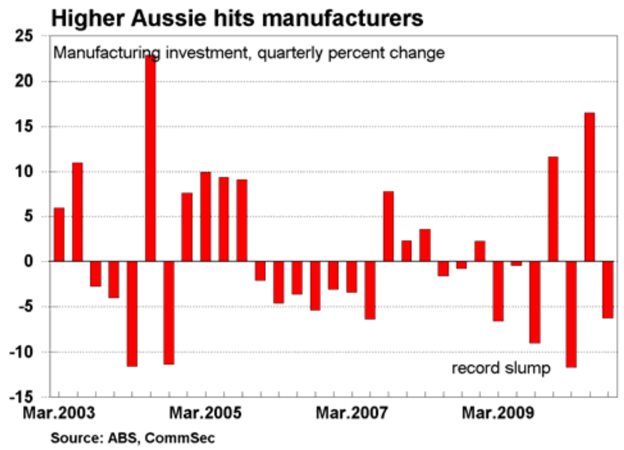


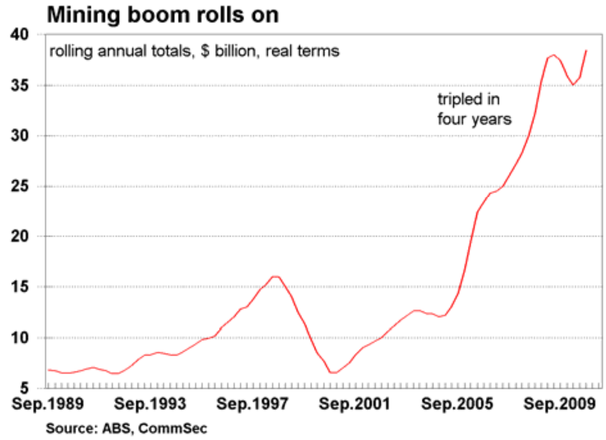
What do the figures show?

- **Business investment** rose by 6.2 per cent after falling by 3.2 per cent in the June quarter. The June quarter result was revised up from the earlier-reported fall of 4.0 per cent. In annual terms investment was up 8.6 per cent on a year ago.
- Spending on buildings rose by 13.4 per cent in the quarter. Spending on equipment fell by 1.1 per cent after sliding by 5.2 per cent in the June quarter.
- Spending in the mining sector rose by 15.6 per cent and fell by 6.3 per cent in “other selected industries”. But investment slumped in the manufacturing sector by 6.3 per cent in the September quarter.
- Investment rose in just one of the eight states and territories in the September quarter. The biggest increase was in NSW (up 15.3 per cent), Western Australia (up 10.4 per cent), and Queensland (up 6.0 per cent). Spending fell most in the Northern Territory (down 14.5 per cent), followed by Tasmania (down 6.8 per cent), South Australia (down 6.0 per cent), ACT (down 5.7 per cent), and Victoria (down 4.0 per cent).
- The overall deflator for investment goods rose by 0.6 per cent in the September quarter after falling by 1.2 per cent in the June quarter. The price of buildings and structures rose by 1.2 per cent in the quarter while the cost of equipment fell by 0.3 per cent.
- Over the year, the cost of investment goods fell by 1.9 per cent. The cost of buildings rose by 1.6 per cent over the year, while the cost of investment equipment fell by 5.6 per cent over the year.
- The fourth estimate of investment for 2010/11 was $123.9 billion, unchanged on the third estimate and slightly below the usual (average) upgrade in the quarter of 6.9 per cent. Compared with a year earlier, the fourth estimate of investment was up 19.5 per cent on a year ago.

What is the importance of the economic data?

- **Private New Capital Expenditure and Expected Expenditure** is released quarterly by the Bureau of Statistics. The figures show actual and expected spending by businesses on tangible assets such as new buildings,





machinery and office equipment. The figures are obtained after sampling 8,000 private business units.

- The data on actual spending is broken-down at a state and industry level and estimates are represented in nominal and price-adjusted (volume) terms. The data on expected spending contains a mix of short and longer-term estimates. The short-term estimates may focus on periods just three months ahead while the longer-term estimates may look as far as 18 months into the future.

What are the implications for interest rates and investors?

- The planned investment data for the September quarter is a little disappointing, however given that the fourth estimate for spending in 2010/11 is up 19.5 per cent on the equivalent estimate for 2009/10 it is unlikely to concern the central bank at this stage.
- Interest rates will continue to rise as the recovery gains traction. However business and consumers will need a few months to adjust to the current economic conditions. Spending and activity needs to be firmly entrenched before interest rates are raised once again.

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