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Capital expenditure

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A capital expenditure is the use of funds or assumption of a [liability](#) in order to obtain or upgrade physical [assets](#). The intent is for these assets to be used for productive purposes for at least one year. This type of [expenditure](#) is made in order to expand the productive or competitive posture of a business. Examples of capital expenditures are funds paid out for buildings, computer equipment, machinery, office equipment, vehicles, and software. An example of an asset upgrade is adding a garage onto a house, since it increases the value of the property, whereas repairing a dishwasher merely keeps the machine in operation. Capital expenditures tend to be quite substantial in certain industries, such as utilities and manufacturing.

A capital expenditure is recorded as an asset, rather than charging it immediately to [expense](#). It is classified as a [fixed asset](#), which is then charged to expense over the [useful life](#) of the asset, using [depreciation](#). For example, if you acquire a \$25,000 asset and expect it to have a useful life of five years, then charge \$5,000 to depreciation expense in each of the next five years. The asset is initially recorded in the [balance sheet](#), while the periodic depreciation charges against it appear in the [income statement](#).

Since there is a record keeping cost associated with capital expenditures, these items are generally charged to expense if they cost less than a certain predetermined limit, which is known as the [capitalization limit](#). For example, if a company's capitalization limit is \$2,000, then a computer costing \$1,999 would be charged to expense in the period incurred, whereas it would be recorded as a fixed asset if it cost \$2,001.

The reverse of a capital expenditure is an operational expenditure, where the cost is incurred strictly for current operations. Always charge operational expenditures to expense when incurred. Since they are charged to expense in the period incurred, they are also known as [period costs](#).

From a financial analysis perspective, a business should at least maintain its historical level of capital expenditures. Otherwise, it will be suspected that management is not adequately reinvesting in the organization, which will eventually lead to a decline in the business.

Similar Terms

A capital expenditure is also known as a capital expense, or as capex.

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Steven Bragg

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