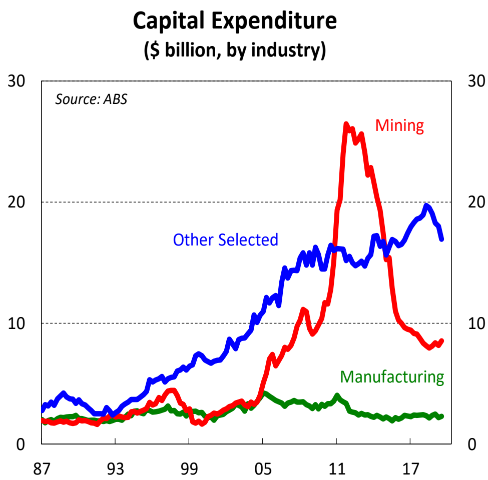
Data snapshot

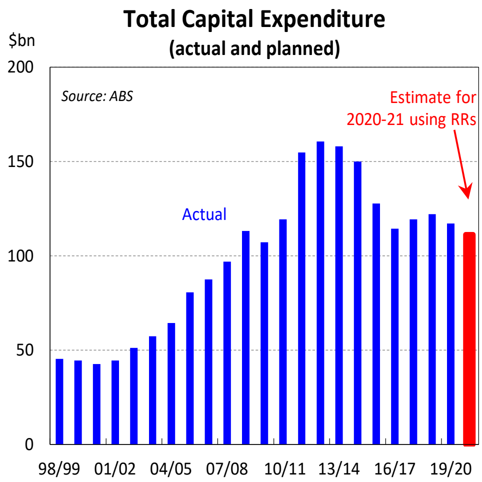
Thursday, 27 August 2020

Private Capital Expenditure

Investment Winds Back

- **Business spending weakened significantly in the June quarter, when widespread lockdown measures were in place at the height of the COVID-19 pandemic. Private capital expenditure (or capex) fell 5.9% in the June quarter, the biggest quarterly decline in just over four years.**
- **A sharp decline was anticipated reflecting the collapse in confidence and extreme uncertainty about the outlook under COVID-19. Businesses are also needing to adjust to major shifts in consumer behaviour and operations, including adhering to social distancing guidelines, increased online activity, a shift away from international travel and working from home arrangements.**
- **The fall in business spending was driven by services or “other” industries, which have been more significantly impacted by COVID-19. Capex for services declined 8.4%, the largest quarterly fall since the June quarter 1993. Spending plans for 2020-21 in this sector also imply a larger fall in spending than other sectors.**
- **Capex fell in the mining and manufacturing sectors. Spending was relatively resilient in the mining sector, declining 1.2% in the quarter. Mining has been less directly affected by social distancing requirements and has been supported by Chinese demand for our commodities.**
- **The third estimate for investment plans in 2020-21 implies a 4.9% decline in spending after a 4.3% decline in the previous year.**
- **Today’s data highlights one of the longer lasting challenges facing the economic growth outlook, even as parts of the country have re-opened after restrictions were in place in the June quarter. Investment spending will likely be weak while uncertainty with COVID-19 developments remain and while confidence remains low.**





Actual Spending

Business spending weakened significantly in the June quarter, when widespread lockdown measures were in place at the height of the COVID-19 pandemic. Private capital expenditure (or capex) fell 5.9% in the June quarter, the biggest quarterly decline in just over four years.

While the decline in investment was not as large as our forecast and median estimates, the sharp decline was anticipated reflecting the collapse in confidence and extreme uncertainty about the outlook under COVID-19.

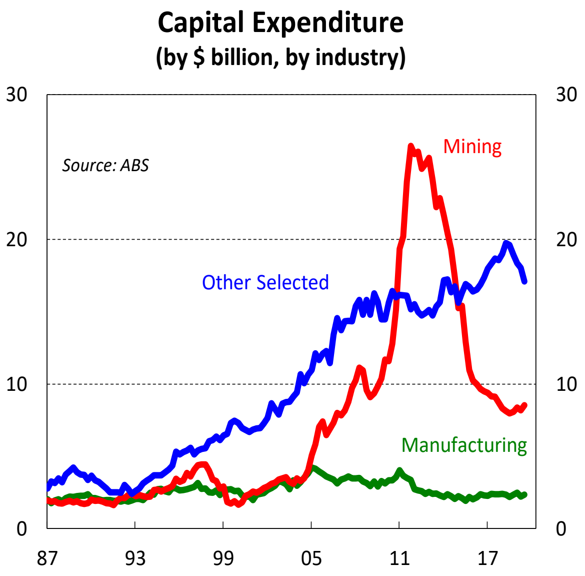
In the RBA's Statement on Monetary Policy, the RBA reported that firms had deferred or cancelled planned investment to preserve liquidity in response to weak current and expected demand. The Australian Bureau of Statistics (ABS) in its business surveys has also reported that 23% of businesses surveyed had decreased or cancelled their actual or planned expenditure.

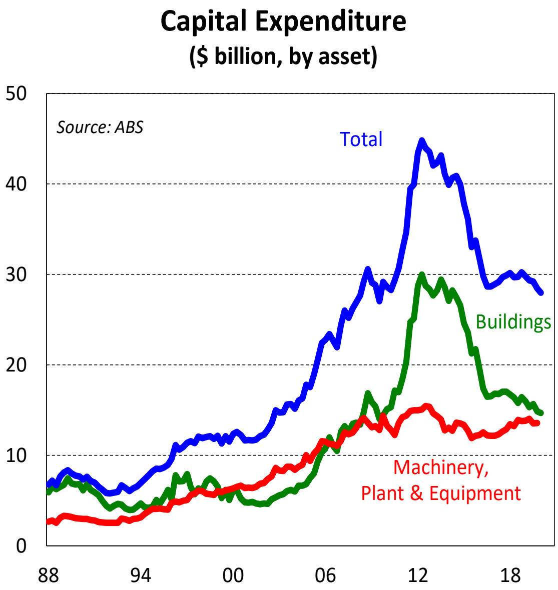
The uncertainty for businesses stems from the unpredictable nature of the virus. In addition, businesses are needing to adjust to major shifts in consumer behaviour and operations, including adhering to social distancing guidelines, increased online activity, a shift away from international travel and working from home arrangements.

The fall in business spending was driven by services or "other" industries, which has been more significantly impacted by COVID-19. Capex for services declined 8.4%, the largest quarterly fall since the June quarter 1993. Tourism and education sectors have been particularly adversely affected by the international border restrictions. We note that investment in services was weak in the lead up to the pandemic. Capex in this sector has declined for six quarters straight. On an annual basis, capital spending in services was down 18.6%, and was the weakest since 1992.

Capex in mining and manufacturing also showed weakness, but to a lesser extent. Manufacturing capex fell 4.5% in the June quarter, while mining capex fell 1.2% in the quarter. While uncertainty about the outlook for the global economy are likely weighing on some areas of mining, the extensive fiscal support from the Chinese government to support infrastructure spending has boosted demand for iron ore.

Across asset classes, spending in machinery, plant and equipment led the decline, falling 7.6% in the quarter, while expenditure on buildings fell 4.4%.





States and Territories

Capex across all States, except for South Australia (4.8%) and the ACT (23.4%) weakened in the June quarter. Unsurprisingly, capex weakened in NSW (-8.9%) and Victoria (-6.3%) which have been most impacted by cases of COVID-19. There were also sizeable declines in capex spending in Queensland (-9.5%), Tasmania (-17.1%) and the Northern Territory (-23.2%).

On an annual basis, capex was in decline in all States and territories, except for Western Australia (7.9%), which is benefiting from the relative resilience of the mining sector. The weakness across non-mining investment was evident across the various States and territories. Annual rates were in decline in NSW (-10.1%), Victoria (-12.9%), Queensland (-7.8%), South Australia (-18.6%), Tasmania (-4.8%) and the ACT (-12.5%). Western Australia (14.3%) had the strongest positive gain, while capex in the Northern Territory (0.4%) was also higher on a year ago.

Spending Plans

Today, we received the third estimate for spending in 2020-21, which was $98.6 billion. This was 8.9% higher than the second estimate received in the previous quarter. However, the third estimate of spending is always typically higher than the second estimate as companies add to their plans as the year approaches. Of greater relevance in assessing the outlook for investment is the comparison with the third estimate of spending for 2019-20. On this basis, the third estimate for investment plans in 2020-21 was 12.6% lower than the third estimate for spending last year.

An alternative for assessing the outlook is by accounting for the differences in the estimates to actual spending outcomes. We can do this through realisation ratios. Using a five-year average of the realisation ratio, the third estimate of spending would imply a 4.9% decline in spending in 2020-21.

We also received actual spending for 2019-20. Total spending declined 4.3% from the previous year.

The breakdown by sectors was in step with the varying degrees of impact from COVID-19. The outlook for services investment was weakest. Capex spending in services (based on realisation ratios) is estimated to be down 19.3% in 2020-21 after a 9.1% decline in 2019-20.

Estimates for manufacturing and mining investment also implied weaker spending than previously (using realisation ratios). Manufacturing investment was estimated to be down 6.8% in 2020-21 after a 1.5% increase in 2019-20. Meanwhile, mining investment is now estimated to have risen 6.1% in 2020-21, down from 11.9% estimated previously.

Outlook

The weakness in investment spending over the June quarter does not come as a surprise given the significant uncertainty about the outlook, weak demand and major shifts in consumer behaviour.

Many businesses continue to face stresses in dealing with a new way of operating. Scaling back or deferring business investment plans is one way in which they can preserve cash in this time of uncertainty.

Today's data highlights one of the more longer lasting challenges facing the economic growth outlook, even as parts of the country have re-opened after restrictions were in place in the June quarter. Investment spending will likely remain weak, while uncertainty with COVID-19 developments remain and while confidence is low.

Janu Chan, Senior Economist
Ph: 02-8253-0898

Contact Listing

Chief Economist
Besa Deda
dedab@bankofmelbourne.com.au
(02) 8254 3251

Senior Economist
Janu Chan
chanj@bankofmelbourne.com.au
(02) 8253 0898

Economist
Nelson Aston
nelson.aston@bankofmelbourne.com.au
(02) 8254 1316