

Australian economic update

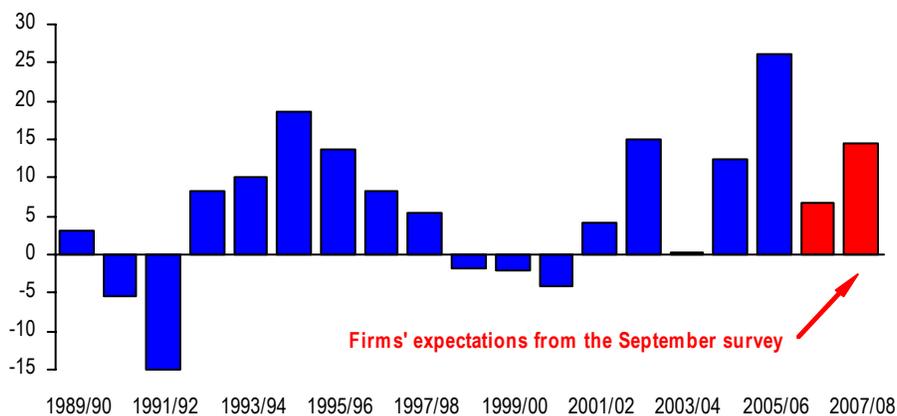
Business investment survey – 3Q

Today's September quarter business survey showed an unexpected 6.5% drop in spending in the September quarter, and a small downgrade to firms' expectations for spending in the year ended June 2008. In the previous survey, managers expected to raise business investment spending by 17%; now, managers expect a 14% rise. The downgrade probably reflects managers' increased anxiety over the durability of the global economic cycle and the tightening in credit conditions. Also, rising domestic interest rates and uncertainty about a change of government at the November 24 federal election may have contributed to the small downgrade.

Investment unexpectedly fell across each of the main industry groups in 3Q. As such, for the first time in four quarters, even investment in the previously booming mining sector fell (down 3.0%q/q). The largest fall, though, was in investment in 'other selected industries' (down 9.3%). Investment in manufacturing, which is struggling under the burden of the rising currency and stiff competition from offshore, fell another 2.1%, to take its stretch of declines to eight straight quarters. The drop in spending in 3Q may be partly explained by the fact that some firms are struggling to gather the required labour and equipment to undertake planned investment projects; this is particularly true in mining and infrastructure.

Business Investment - total

Nominal, annual % change, FY



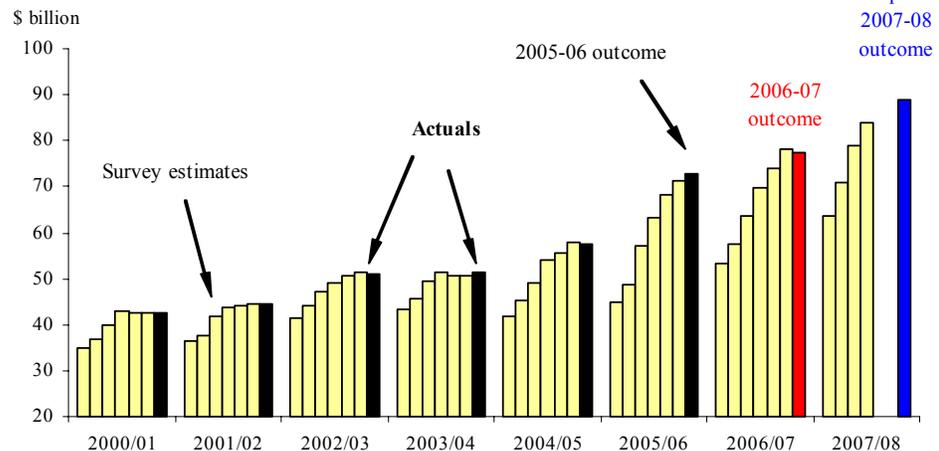
The forward looking component of this survey always is more important than the historical print. Firms' fourth (of seven) estimate of spending for the fiscal year ended June 2008 showed that managers expect to raise investment spending by a still-healthy 14% relative to 2006-07, after adjustment for firms' usual estimation errors (using 5-year average realization ratios). This represents a slight downgrade relative to the 2Q survey.

Even with today's modest downgrades to firms' investment plans, though, Australia's private investment outlook is rosy. Firms expect to raise their investment spending at a double digit pace in 2007-08 despite this investment cycle being at a very mature phase; firms have raised their investment spending for the last six years. In fact, business investment in real terms has increased 73% since 2003-04. From the RBA's perspective, adding to the country's productive capacity should help to alleviate pressure on stretched resources which, in the long term, should help to ease inflation pressure.

The details:

- Business investment unexpectedly dropped 6.5%q/q in real terms in 3Q (JPMorgan 3.5%, consensus 2.0%), after a revised 7.1% rise in 2Q. The biggest drop was in spending on buildings and structures (-9.4%q/q). Spending on equipment and machinery fell 2.3%.
- Firms' fourth estimate of spending in the year ended June 2008 printed at \$83.8 billion, which implies a 14% rise relative to spending in 2006-07. This is a small downgrade from the implied 17% rise in the previous survey.

Private new capital expenditure



Business investment by type of asset

\$ million, constant prices, seasonally adjusted

