THE ALLEASING

EQUIPMENT DEMAND INDEX

CAPITAL CONSTRAINTS A COMMON COMPLAINT

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AUSTRALIA

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Businesses aspire to grow and expand, but often the financial resources to do so are out of reach. Internal funding sources, from cash flow or equity from shareholders, are often not enough to fund ambitions for growth, whether that be through a mergers and acquisition (M&A) process or other expansion strategies.

Even in a low interest rate environment, with banks and investors searching for returns, Australian businesses are struggling to access the capital they need to fund their plans for growth. The Alleasing Equipment Demand Index, (the Index) found that capital constraints are restricting the ability of 28.2 per cent of businesses to grow and function efficiently. This was particularly acute in the lower corporate segment of businesses, with revenues between $21 and $100 million a year, where the figure was a full 30 per cent.

Of those businesses struggling with capital constraints, more than half (52.4 per cent) said they had had fundamental problems accessing sufficient capital. Banking providers, capital markets and investors, appear to either have too much demand on limited funds or, consider many businesses to be outside of acceptable risk parameters.

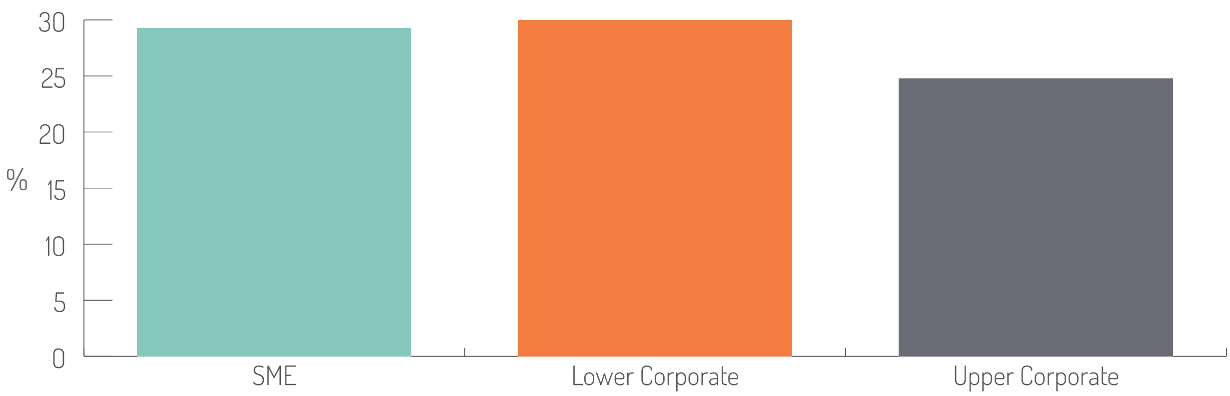
The reality is that while many businesses have a vision for their future, they struggle to present that vision effectively enough to convince investors.

Feedback from the businesses interviewed for the Index, showed that many believe there are inherent inefficiencies in how capital is distributed in the Australian market. The research also uncovered evidence of the uncertainty which currently prevails in global markets. Several respondents, namely Australian subsidiaries of parent companies in Europe, the US and Japan, cited a lack of investment funds from head of finance as their major issue.

The interviews pinpointed the impact that the capital constraints were having on businesses. Businesses suffering from capital constraints (35.5 per cent) said they would like to pursue an M&A deal, but lacked access to the funds to do so. Of those businesses with a turnover between $5 to $250 million per annum, 10 per cent are frustrated that they haven't been able to participate in an M&A deal. Unlocking even a portion of that pent up demand would have a significant impact on the financial industry and the wider economy.

NB For any business, a lack of capital means underinvestment in their existing plant and equipment. Of those businesses, 28.2 per cent of businesses struggling with access to capital, 12.1 per cent said the result was that they were struggling with old equipment which was hampering their efficiency and ability to grow.

Percentage of Businesses Constrained by Capital



SENTIMENT PAUSES FOR BREATH. ARE FEARS OF A RECESSION OVERDONE?

The vital signs for the health of the Australian economy are ambiguous. Growth figures before the end of 2016 sparked speculation that the economy could be headed for its first recession in a quarter of a century, but this was seemingly dispelled by an unexpected trade surplus.

Initially, economic observers were surprised by the 0.5 per cent fall in national GDP in the September quarter of 2016. According to the Australian Bureau of Statistics (ABS), the annual growth rate came in lower than expected at 1.8 per cent, with public capital spending, private building investment and net exports reporting sharp falls.

This represented the Australian economy's worst performance since the Global Financial Crisis of 2008, and was the fourth time growth had been in negative territory in the last 25 years.

Just as economists were speculating on a second quarter of negative growth, the technical definition of a recession, came the best balance of trade figures in almost three years. The ABS figures showed a trade surplus of $1.24 billion off the back of higher coal and iron ore prices, and are now expected to drive a return to growth.

Even so, the economic outlook is uncertain, and the Alleasing Equipment Demand Index is a reflection of this ambivalence. While 25.6 per cent of businesses across the nation say they plan to increase their asset base in the first quarter of 2017, the actual increases in the size of the asset base are lower this round, at 6.5 per cent, against the 8.0 percent reported in October.

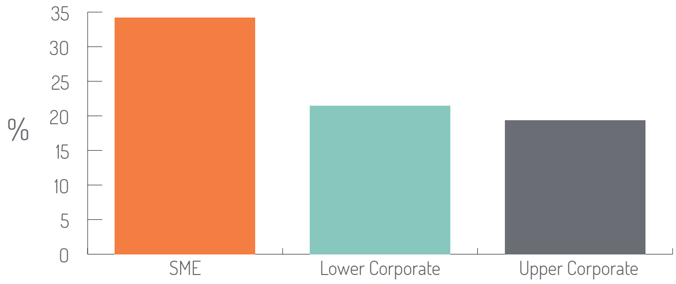
The best comparison is in the segment of lower corporate businesses, or those with revenues of between $20 and $100 million a year. The percentage saying they will increase their asset base has moved from 18.9 per cent in October to 21.5 per cent this round, while the actual increase has gone from 5.8 per cent to 5.1 per cent over the same period. SME businesses, or those with revenues of $5 to $20 million, are the most bullish, with 34.0 per cent planning an increase, but the rate of increase has also fallen from 8.6 per cent to 7.8 per cent.

For the first time, the Index now includes the upper corporate segment of businesses with annual revenues of $101 to $250 million. This segment proved to be the least bullish, with a significantly lower 19.4 per cent indicating they plan to increase assets, by a lower than average 5.3 per cent.

The picture which emerges is of a business sector which is caught between a natural desire to expand, but is cautious about over committing in an environment of uncertainty. Australia is caught between domestic economic forces – with an ongoing argument for more cuts in official interest rates to stimulate growth – while globally, momentum is growing for a change in the interest rate cycle.

The current Index delivers a snapshot of Australian businesses pausing for breath as they ponder how economic forces will play out in the first months of 2017, and the first months of the Trump Presidency in the US.

Percentage of Businesses Intending to Increase Asset Base in Q1 2017



A TALE OF A MULTI-SPEED ECONOMY

The ABS GDP growth figures for the September quarter of 2016 pinpointed a wide disparity in the economic performance of the states which is also reflected in the Alleasing Index.

Beyond geographies, the Index also shows significant differences in sentiment between industry sectors, reinforcing the view of an uneven economy traveling at different speeds.

ABS figures also state that while GDP fell by 0.5 per cent on a national basis, there was a 3.8 per cent decrease in Western Australia after a 2.7 per cent fall in the June quarter.

According to the Index, only 16.5 per cent of Western Australian businesses intend to increase their asset base in the first quarter of 2017, well down from the national average of 25.6 per cent.

In New South Wales, the economy grew a marginal 0.1 per cent, after a much stronger 1.6 per cent increase in June, according to the ABS figures. The Index also found the state's businesses to be the most bullish nationally, with 30.0 per cent planning to increase their asset base during the March 2017 quarter.

South Australia, which is reported in the Index with the Northern Territory (where GDP grew 4.7 per cent in the September quarter), was less bullish but 22.2 per cent of businesses are still planning to increase their asset base.

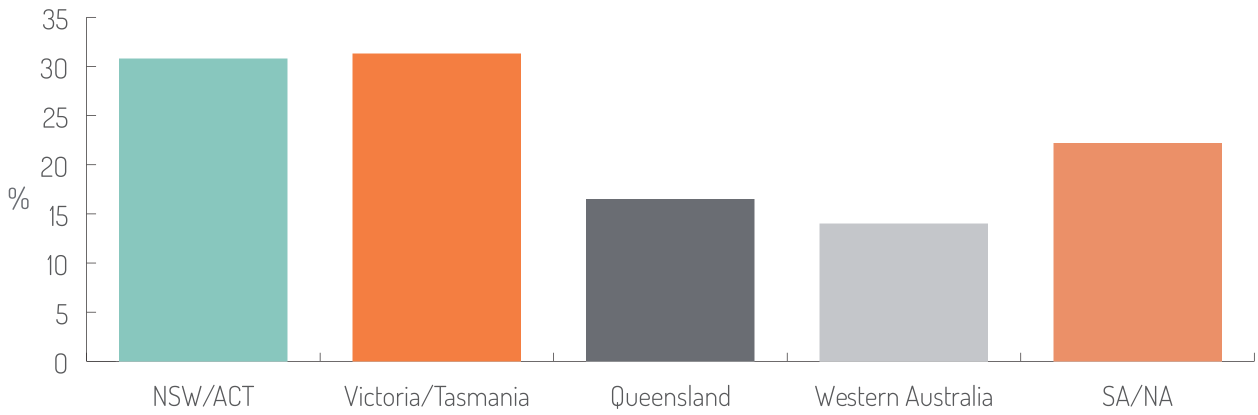
Queensland remains something of an enigma. Although September quarter growth of 0.1 per cent was the same as New South Wales, Queensland's annualised growth of 1.2 per cent is below the national average of 1.8 per cent, and the ABS figures show a significant slowdown in the latter part of 2016.

The Alleasing Index identified a cautious sentiment among Queensland businesses, with 16.5 per cent planning to increase their asset base, putting the state fourth out of the five regions surveyed.

Amongst the industries surveyed, mining and construction are the most bearish, with 17.4 per cent of mining companies planning to increase their asset base, whereas transport, agriculture and manufacturing are the most optimistic.

Thirty per cent of businesses in the transport and storage sector, for example, say they plan to increase their asset base during the March quarter 2017, while only 20.0 per cent of construction firms are planning to do so.

Percentage of Businesses Planning to Increase Asset Base by State



THE ‘INTERNET OF THINGS’ ERA BEGINS

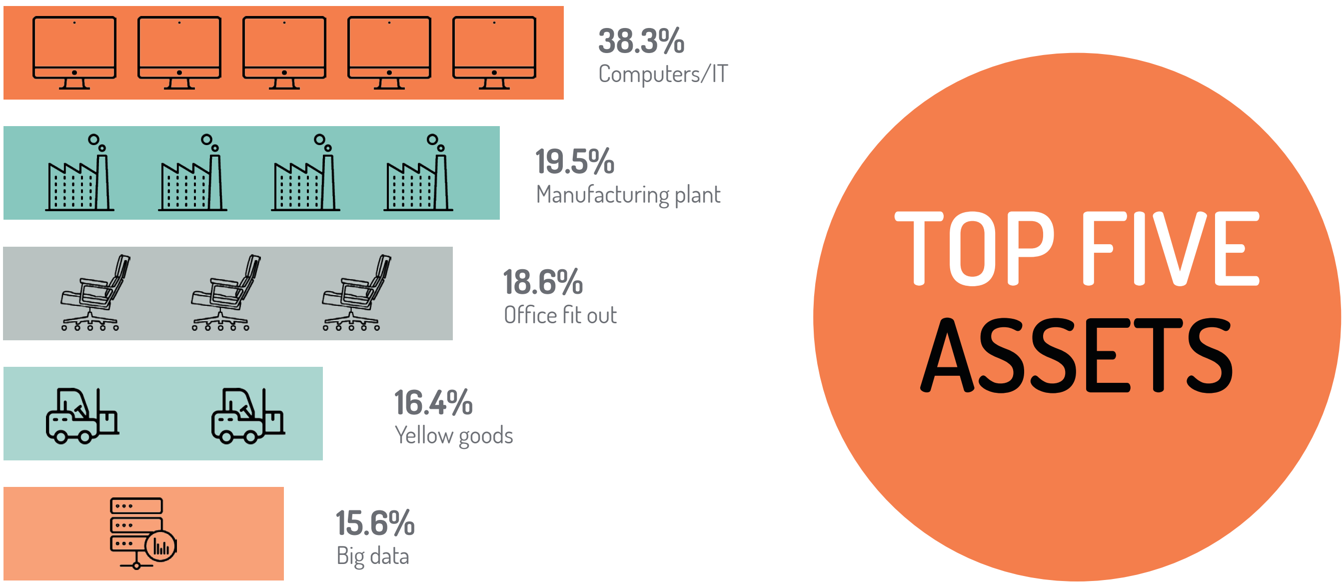
The connected ‘Internet of Things,’ (IoT) world is not simply one technology, it is a combination of wireless, cloud services, mobility and data analytics. So far, 2017 is shaping as a significant milestone year in its development as devices across the globe connect online.

Technology giant Cisco says that while there are around 10 billion devices connected to the internet today, that could grow to as many as 50 billion by 2020 as wireless links move beyond smartphones and computers.

The Alleasing Index routinely tracks the assets which Australian companies are planning to acquire, and this round shows a growing diversity underlining the emergence of the IoT world. Alongside acquisitions such as cars, trucks and computers (see below), the Equipment Demand Index has revealed that the most popular assets that Australian businesses acquire are IT services for managing big data, drone technology and process automation services, all of which play into the IoT future.

Big data is a clear focus. With so many new devices coming online, the amount of data created and collected with the need to be analysed, will increase exponentially. According to the Index, 15.6 per cent of the Australian businesses who say they plan to increase assets in the first quarter of 2017 say they are focused on big data technology and services.

Intentions around other related technologies are significantly lower, but play into a similar story. Of those businesses who are looking to invest in technology, 3.1 per cent of companies say they will acquire drone technology, 3.1 per cent cite process automation, while 1.6 per cent nominate artificial intelligence. These are baseline starting points, but resonate with priorities around big data, and suggest that 2017 will be a year when the IoT begins to gain traction.



NB. Some businesses are acquiring multiple assets

IN SUMMARY

The Alleasing Equipment Demand Index continues to mirror key Australian Bureau of Statistics data. The ABS data series on equipment, plant and machinery investment showed a 3.5 per cent uptick in the September 2016 quarter, against only 1 per cent in June. Through our own research, the same results have been found and can be seen reflected in the Alleasing Index outcomes, with a higher percentage of businesses, 25.6 per cent, indicating they plan to increase their asset base during the March quarter 2017.

But while the number of businesses planning to increase assets is higher, the percentage increase in the asset base has moved lower (at 6.5 per cent). Key states and major industry sectors continue to lag these averages, suggesting that Australian business – and the wider economy – moves into 2017 with some ambivalence.

2016 was a tumultuous year in global terms. Economically there was the Brexit shock in the United Kingdom, the surprise election of Donald Trump in the United States and – in our region – concerns about a slowdown in the Chinese economy. In addition, geopolitical issues in the Middle East added new layers of risk. While the damage to the global economy was not as severe as some forecasted, the cumulative effect spread uncertainty and a fear of volatility. Many of these same issues will have an impact, and perhaps a larger influence in 2017.

Australian businesses are not immune from these factors. The Alleasing Index presents a picture of businesses wanting to grow and transform, but they are uncertain on how much they should commit to the course for growth. SME businesses are arguably the engine of the economy and the data shows they are the business segment with the strongest appetite for increasing their asset base, but they face consistent headwinds. Many businesses struggle with the constraints of senior debt in some form, however, limited access to capital alongside unproductive assets, restricts their ability to optimise efficiency and execute strategic plans for growth.

Economic volatility, interest rate rises, and ongoing issues around access to capital are undermining otherwise positive business confidence as we move into 2017. Economic forecasters believe that the Q4, 2016 GDP figures will recover and Australia will avoid recession but even if they are proved correct, business sentiment became cautious at the end of 2016 as it contemplated the year ahead.

ABOUT

The Alleasing Equipment Demand Index is a quarterly index, which examines the current asset inventory of Australian businesses, as well as expectations for future investment. The inaugural index was run during July and August 2014.

For the first time, this edition of the Index includes 'Upper Corporate' businesses turning over between $101 million and $250 million each year. The Index comprises research from three segments: SME's turning over $5-$20M, Lower Corporates ($20-$100M), and Upper Corporates ($100-$250M).

This round of the index was created from interviews with 500 Australian businesses in December 2016.

The index is executed by Collins Communications on behalf of Alleasing.

Alleasing is a leading, independent provider of asset finance and leasing solutions. Established more than 25 years ago, we have financed billions of dollars' of assets across a range of sectors, and business sizes.

Our focus is on supporting businesses to achieve greater productivity and growth through effective management of their assets, and we are prepared to invest in helping you do this via a residual position in the assets.

Our team is driven to deliver solutions that meet your business needs and which provide operational flexibility. This includes the ability to acquire, change or expand your asset base as the need arises alleasing

Sydney | Melbourne | Brisbane | Perth

P 1300 134 214

E enquiries@alleasing.com.au

alleasing.com.au