

CAPITAL SPENDING OUTLOOK FOR 2016

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Although growth is expected in the U.S. manufacturing sector this year, some companies are taking a “wait and see” approach to capital expenditures (CAPEX) due to falling oil prices, the economic slowdown in China, the U.S. stock market’s rocky start in 2016, and potential policy changes resulting from the presidential election.

SLOW BUT STEADY GROWTH PROJECTED

The Congressional Budget Office projects that the U.S. economy will see solid expansion in 2016 and 2017. In 2016, it forecasts real (inflation-adjusted) U.S. gross domestic product (GDP) growth of 2.7%, an increase over the 2015 growth rate of 2.0%.¹

In a recent survey of purchasing and supply management executives by the Institute for Supply Management (ISM), respondents expect 2016 revenues to increase in 16 manufacturing industries and 15 non-manufacturing industries.² Capacity utilization is up, with respondents in the manufacturing sector operating at 81.6% of normal capacity and non-manufacturing respondents operating at 87.9% of normal capacity.³

MIXED OUTLOOK FOR CAPEX SPENDING

These projections are positive signs of economic stability, yet a degree of uncertainty lingers with some corporate executives. Additional interest rate hikes are widely expected in 2016, and the U.S. dollar continues to be strong against major world currencies, both of which could increase borrowing costs and reduce revenues.

Some of this uncertainty runs along business sectors. In ISM’s most recent survey, manufacturing members forecast only a 1.0% increase in CAPEX, while non-manufacturing members project 7.5% growth.⁴ Most respondents noted that the strength of the U.S. dollar will likely have little or no impact on their capital investment plans this year.⁵

The Equipment Leasing and Finance Association (ELFA) projects that U.S. companies will invest \$1.627 trillion in plant, equipment and software in 2016, with 64% of capital investment financed through loans, leases and lines of credit.⁶ ELFA notes that the expectation of additional interest rate hikes this year may spur small to mid-size businesses to make capital investments sooner to take advantage of lower rates before they rise further.⁷

ELFA notes that some sectors are growing, such as construction, medical equipment, computers and software. Other sectors — such as agriculture, mining, oilfields, railroads, industrial and materials handling equipment — have a weaker economic outlook with correspondingly low CAPEX investment anticipated



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The Gartner Worldwide IT Spending Forecast calls for global IT spending to be relatively flat at 0.6%, but data center spending is expected to increase by 3.0% to \$75 billion.⁸ The U.S. healthcare sector is likely to play a major role in IT spending this year. Increased scrutiny of healthcare costs, advances in medical techniques and growing cybersecurity threats are pushing hospitals and health systems to invest in new computers, medical technology, data analytics and software to standardize care, track medical spending, measure health outcomes and substantiate reimbursements.⁹

Low oil prices are expected to continue throughout the year and this will limit investment in traditional energy equipment and technology.

The oil and gas sector expects the sharpest declines in CAPEX due to depressed oil prices, production shutdowns, over-capacity and ongoing price volatility. Oil and gas CAPEX should drop by 20% to 25% in 2016.¹⁰

ANOTHER WILD CARD: THE 2016 PRESIDENTIAL ELECTION

The upcoming U.S. presidential election may also impact companies’ decisions on capital investment, as a change in leadership and party affiliation could spell major changes in several U.S. policies. This is leading some companies to use scenario planning when trying to decide on the budget and timing of their CAPEX spending this year.

To discuss these topics in more detail, please contact your PNC Relationship Manager.

1 Summary of “The Budget and Economic Outlook: 2016 to 2026,” Congressional Budget Office, Jan. 19, 2016. Available at: https://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/51129-2016_Outlook_Summary.pdf

2 “Economic Growth Continues in 2016,” press release from the Institute for Supply Management, Dec. 8, 2015. Available at PR Newswire at: <http://www.prnewswire.com/news-releases/economic-growth-continues-in-2016-manufacturing-growth-expected-in-2016-revenue-to-increase-41-capital-expenditures-to-increase-10-capacity-utilization-currently-at-816-non-manufacturing-growth-projected-in-2016-revenue-300189385.html>

3 “Economic Growth Continues in 2016,” press release from the Institute for Supply Management, Dec. 8, 2015. Available at PR Newswire at: <http://www.prnewswire.com/news-releases/economic-growth-continues-in-2016-manufacturing-growth-expected-in-2016-revenue-to-increase-41-capital-expenditures-to-increase-10-capacity-utilization-currently-at-816-non-manufacturing-growth-projected-in-2016-revenue-300189385.html>

4 “Economic Growth Continues in 2016,” press release from the Institute for Supply Management, Dec. 8, 2015. Available at PR Newswire at: <http://www.prnewswire.com/news-releases/economic-growth-continues-in-2016-manufacturing-growth-expected-in-2016-revenue-to-increase-41-capital-expenditures-to-increase-10-capacity-utilization-currently-at-816-non-manufacturing-growth-projected-in-2016-revenue-300189385.html>

5 “Economic Growth Continues in 2016,” press release from the Institute for Supply Management, Dec. 8, 2015. Available at PR Newswire at: <http://www.prnewswire.com/news-releases/economic-growth-continues-in-2016-manufacturing-growth-expected-in-2016-revenue-to-increase-41-capital-expenditures-to-increase-10-capacity-utilization-currently-at-816-non-manufacturing-growth-projected-in-2016-revenue-300189385.html>

6 “ELFA Announces Top 10 Equipment Acquisition Trends for 2016,” Jan. 12, 2016. Available at: https://www.elfaonline.org/news/IndNews/news_report.cfm?id=22301

7 “ELFA Announces Top 10 Equipment Acquisition Trends for 2016,” Jan. 12, 2016. Available at: https://www.elfaonline.org/news/IndNews/news_report.cfm?id=22301

8 “Gartner Says Worldwide IT Spending Outlook is Forecast to Grow 0.6 Percent in 2016,” Gartner press release on Jan. 18, 2016. Available at: <http://www.gartner.com/newsroom/id/3186517>

9 “2016 Global Health Care Outlook: Reconciling Rapid Growth & Cost Consciousness,” The Carlyle Group. Available at: https://www.carlyle.com/sites/default/files/market-commentary/october_2015_-_global_health_care_investment_outlook.pdf

10 “Moody’s Sees Oil and Gas Capex Down 20% to 25% in 2016,” by Paul Austick, *24/7 Wall Street* blog, Jan. 4, 2016. Available at: <http://247wallst.com/energy-economy/2016/01/04/moodys-sees-oil-and-gas-capex-down-20-to-25-in-2016/>

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CIB ENT PDF 0216-0100-239002