Capex: India Inc has to do its part

INVESTMENT THRUST. Government has been doing much of the heavy lifting on investment in recent times. It's time the private sector stepped up

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With the Union Budget likelyto be presented in July, there are a plethora of expectations and suggestions being made to the government.

But one common suggestion is asking the government to spend more on capex. This is significant because normally investment is in the purview of the corporate sector (which includes PSUs). This opens the discussion on whether the corporate sector is passing the buck and not doing its bit.

In FY24, the national gross fixed capital formation expenditure was t91-laldi crore which is around 31 per cent of the GDP. Assuming the FY25 GDP is around 1328-lakh crore and the investment ratio remains unchanged, the amount of capital formation would be around t102-lakh crore.

The Interim Budget had targeted a capex of t 11.11-lakh crore for the year, which would be 11 per cent of total capital formation. There are two questions here — how much can 11 per cent of the total drive overall investment and second, how much more does India Inc want the government to do.

Data on the Centre's capex is quite illuminating. The government increased total capex from 13.36-lakh crore in FY20, just before Covid struck, to t11.11-lakh crore for FY25. This is a multiple of 3.3 times.

So there has been considerable advancement made here. But this was made possible also by the increase in government borrowings from 19.33-lakh crore in FY20 to t15.55-lakh crore in FY25. This was the result of the fiscal deficit ratio also moving up sharply from 4.6 per cent of GDP in FY20 to 9.2 per cent in FY21 and then gradually rolled back to 5.1 per cent in FY25.

This was the time the government had to spend in a bigway on both welfare schemes (NREGS, PM-Kisan, housing, free food etc.) as well as capex to keep the economy moving at a time when the private sector was not in a position to do so.

FISCAL PRESSURES

Quite clearly this accelerated pace of growth in capex cannot be sustained forever. While the government can increase its outlay, the pressure of maintaining the fiscal deficit at acceptable levels (4.5 per cent by FY26 and probably 3 per cent in the subsequent three years) would place some limits on the same.

The government would have to balance the two objectives of maintaining social welfare outlays till such time that there is more employment created (which will be in the private space as this is where jobs are created with capex).

Further it should be noted that capex has been concentrated mainly in roads, railways and defence. Executing large projects can also run into capacity issues given that India has a federal set up and land acquisition is a challenge even for national highways projects.

Logically the onus of investment has to be on the corporate sector. Interestingly NSO data on contributors to gross fixed capital formation shows that the corporate sector has a dominant share of 44 per cent followed bythe household sector with 42 per cent for FY23. For the household sector, dwellings accounted for 70 per cent of total capital. Here it must be pointed out that a major boost to housing has been provided by the government in the Budget, through the PM Awas Yojana, not through capex.

> Due to fiscal constraints the Centre cannot sustain the current levels of capex. Given the strong growth prospects, the corporate must step up to the plate

Hence there has been progressive indirect contribution to capital formation by the government through the household sector.

Data on growth in gross fixed capital formation throws light on the relative pace of growth across sectors. For the system as a whole CAGRwas 11.5 per cent for the period FY18-FY23. In case of both the PSUs and private players growth was lower than this average while itwas higher for the government and household sectors.

Therefore, the corporate sector needs to take charge here and not always look for the government to provide acceleration. For the corporate sector, investment decisions crucially hinge on return on investment, so business considerations override all other factors.

In case of the government this is not the case, as money spent is based on necessity and while there is now a clear direction on monetising assets that have been created, profitability is not the chief concern.

CAPACITY UTILISATION

Currently, the corporate sector's average capacity utilisation was 76.5 per cent as of March, as per the RBI. This number is impressive as normally a ratio of 78-80 per cent triggers fresh investment.

However, based on the companies' investor presentations, it can be seen that industries which are linked to infrastructure have witnessed steady growth in investment, which include steel, cement, chemicals, and machinery.

There also seems to be an absence of demand revival in the last two years due to lower rural incomes and high inflation, which has eroded purchasing power. So FMCG and durable goods companies are unlikely to invest till economic conditions improve.

The conclusions that can be drawn are that while the government does play the role of engine to drive infra industries' growth by providing the initial push, there is need for the corporate sector to accelerate their plans.

Prospects for GDP growth in the next five years are bright and it can be said with reasonable confidence that it would average around 8 per cent. Hence, there is reason to invest across sectors.

The clue is employment generation which generates income and consuming power. But it is the private sector, especially manufacturing that has to invest as well as create jobs to lead to a virtuous self-fulfilling cycle.

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