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ECOSCOPE
The Economy Observer

Will corporate capex pick up after elections?

May be, may be not

- **According to the official statistics, corporate (public + private financial and non-financial companies) capex in FY23 was 14.8% of GDP, better than its two-decade low of 12.9% of GDP in FY21, but the same as in the pre-pandemic years (FY17 to FY20) and much lower than its all-time peak of 21.6% of GDP in FY08. This single set of data holds the answers to two very important questions, which dominate the current economic discussions in India:**
  1. **Notwithstanding a four-decade low household net financial savings (HHNFS), why isn't India's current account deficit (CAD) wider?**
  2. **Will corporate capex pick up after 2024 general elections, assuming political stability prevails?**
- **The first question pertains to the present (and the recent past), while the second question is speculative regarding the future. Because of an absence of a widening in India's CAD, many analysts have dismissed the collapse in HHNFS. However, one must remember that CAD represents the entire economy's behavior, and household sector is only a subset of an economy. The answer to the first question lies in the sea change witnessed in the behavior of India's corporate sector post the great financial crisis (GFC) of 2008. Corporate investments in India took a sharp dip post-GFC, falling from its peak of 21.6% of GDP in FY08 to around 17% of GDP over the next few years (up to FY16), before it took another south bound move toward 15% of GDP in the run-up to the pandemic *(Exhibit 1)*.**
- **At the same time, corporate savings fell from 14% of GDP in FY08 to about 11% of GDP in the immediate years post-GFC, but has picked up back to 14% of GDP since FY15 (it averaged 13% of GDP between FY19 and FY21). In FY23, corporate savings are estimated at 14.1% of GDP, same as in FY22 *(Exhibit 2)*. It means that while corporate investments are way off their peak (or a decade ago) levels, corporate savings are almost the same as its pinnacle seen in FY08.**
- **Consequently, the corporate sector has turned from a huge net borrower (i.e., higher investments vis-à-vis savings) till early-2010s to a marginal borrower in recent years. At its peak, the net borrowings of the corporate sector amounted to 7.7% of GDP in FY08, which came down to 3% of GDP between FY14 and FY16 *(Exhibit 3)*. During the past seven years (including the pre- and post-pandemic years, i.e. FY17-FY23), its net borrowings have averaged only 0.8% of GDP, with 0.1% of GDP in FY22 and 0.7% of GDP in FY23. At one hand, lower net borrowings of the corporate sector reflects their muted confidence (or the need) to invest; on the other hand, it represents the space available with the corporate sector to push its capex, as and when they decide to.**
- **In any case, it's the weak corporate investments (or lower borrowings on their part) which is keeping India's CAD contained, despite a sharp decline in HHNFS. If HHNFS remains low (to which many commentators don't give too much importance right now) but the corporate investments pick up (as is almost unanimously believed), CAD will undoubtedly widen. This is exactly what happened in all three previous episodes of investment recovery in India in late 1980s, mid-2000s and early 2010s *(Exhibit 4)*. As India's investment rate (as % of GDP) increased to 26% in FY91 from 20% in FY87, CAD widened by 1.2 percentage points (pp) of GDP, contributing about 20% to the pick-up in investment. The contribution of foreign savings (or CAD) increased to 32% during the mid-2000s (as investment rate picked up to 38.1% of GDP in FY08 from 26.8% in FY04, CAD widened by 3.6pp of GDP) and further to 43% during the post-GFC episode (investment rate was 39% of GDP in FY12 from 34.3% in FY09, and CAD widened by 2pp of GDP during this period).**
- **This brings us to the second question: *Will corporate capex pick up strongly from FY25 onwards after the elections are over, and assuming political stability?* Like most of the times, we resort to historical data to answer this question and while it doesn't take our hopes away, it also certainly does not provide a lot of enthusiasm *(Exhibit 5)*. A look at the movements in corporate capex – in nominal terms – in the pre- and post-election two-year periods since 2004 confirms that while it picked up strongly in the post-election period vs. pre-election period in 2004 and 2009, the growth difference was not significant in the last two elections (i.e., 2014 and 2019).**

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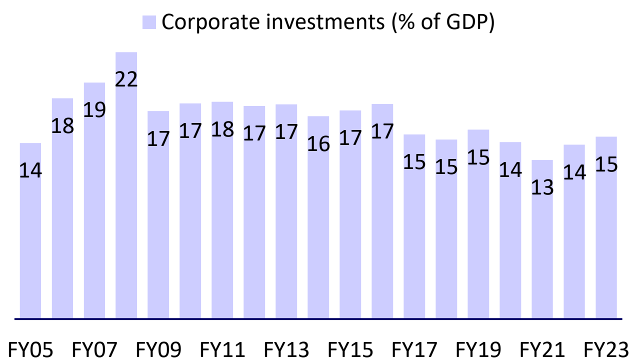
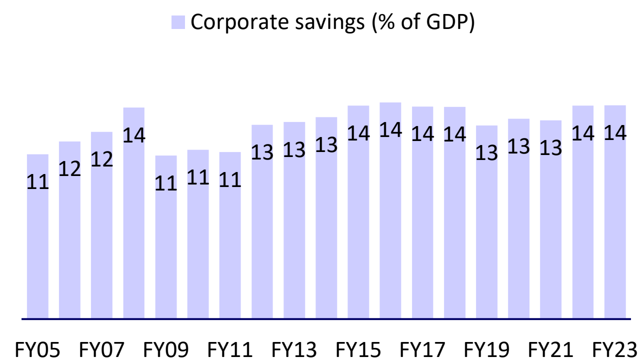
- **One of the clear limitations of such analysis is that many election years in India coincided with other important developments, which, at least to some extent, cloud this analysis. 2004 was the inflection point for India (and the World), coming out from a slow-growth at the turn of the century to the best-ever growth period. 2009 was immediately after the GFC (FY09 was the pre-election year and FY10 was the post-election year for India). Again, 2014 was the year immediately after the 'Taper tantrum' and while pre-2019 was a more normal period, the post-2019 period was affected by the pandemic in early 2020 (that's why we have used FY20-FY23 average for post-2019 election period).**
- **Although this analysis of performance of corporate capex during the pre- and post-elections comes with major riders, there are two key takeaways: a) that post-election growth in corporate capex has been better than the pre-election growth in three of the last four elections, and b) that there was only a marginal pick-up in growth post-2014 elections, and corporate investments grew slowly after 2019 elections (based on FY20-FY23 average). The last two elections, I believe, hold more weight than 2004 and 2009 to understand the potential scenario post-2024 elections.**
- **Further details suggest that PSU investments exhibit greater volatility compared to those in the private corporate sector. In 2014, the recovery in corporate investments in the post-election period was largely driven by PSUs, while the same sector was responsible for the weak growth in the post-election period in 2019 *(Exhibit 6)*. The average growth in private corporate investments during the pre- and post-election period in 2014 and 2019 was narrow-ranged, between 11% and 13%. However, the growth in PSUs capex moved wildly, as it picked up strongly in the post-election period in 2014 and weakened dramatically post-2019 election.**
- **Overall, thus, historical data (especially the last two elections) do not confirm any strong pick up in corporate capex in the post-election period. However, it could still happen if the central government decides to go back to pre-2021 arrangement; pushing the capex through PSEs, as it focuses on the fiscal deficit consolidation. If so, even though corporate capex improves, it will only offset lower government's capex. At the same time, if the private corporate capex also picks up after election, we must be well aware of the constraint posed by lower HHNFS, as a benign CAD could go out of hand very quickly.**

Exhibit 1: Corporate capex in FY23 was similar to that in the pre-pandemic years, but lower than in FY08…



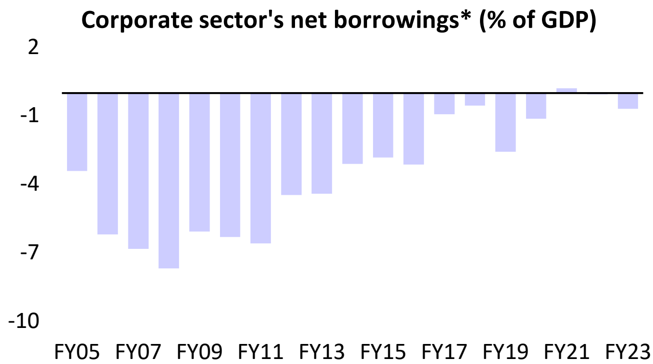
Including private and public financial and non-financial companies 2004-05 up to FY11; 2011-12 base since FY12

Exhibit 2: …however, corporate savings in the past many years are closer to FY08 peak



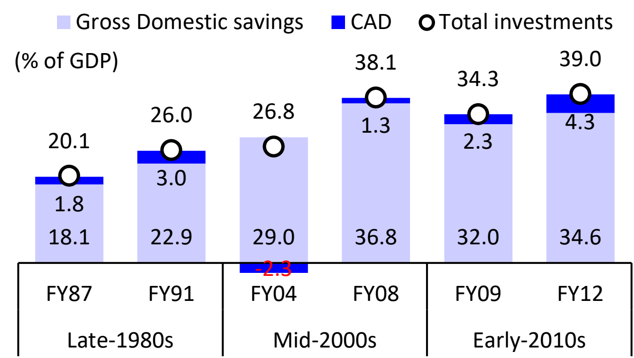
Source: Central Statistics Office (CSO), Reserve Bank of India (RBI), CEIC, MOFSL

Exhibit 3: Corporate sector has moved from a large net borrower to only a marginal one in recent years



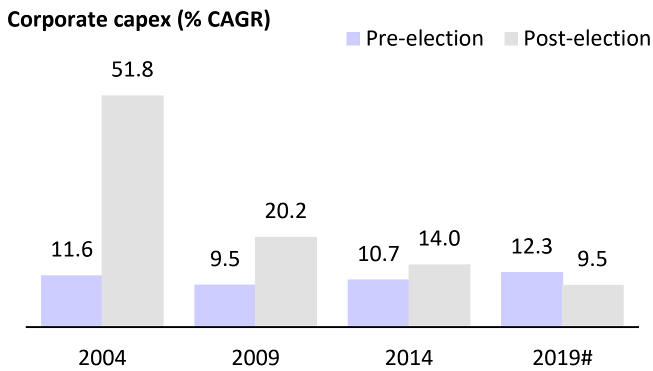
*Savings – Investments

Exhibit 4: Investment recovery in the past has always been supported by wider CAD



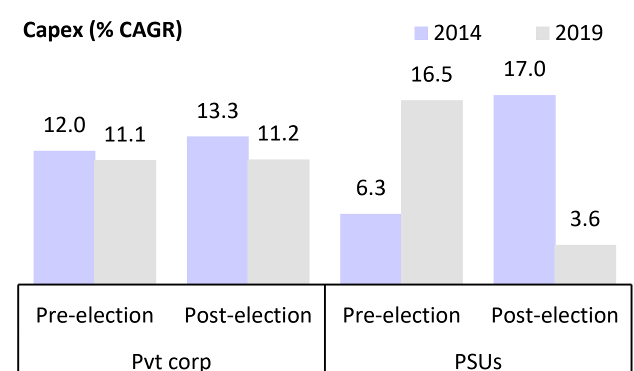
A 'negative' CAD means current account surplus
Source: CSO, RBI, CEIC, MOFSL

Exhibit 5: A comparison of corporate investments in the pre- and post-election periods since 2004



Pre- and post-election period in 2004 was FY03-FY04 and FY05-FY06, respectively and so on except post-2019 period
#Because of the pandemic, post-2019 period is FY20-FY23 average

Exhibit 6: Public corporate capex has weakened materially in post-2019 election period



Pre-election 2014/2019 period = FY13-FY14/FY18-FY19; Post-election 2014/2019 period = FY15-FY16/FY20-FY23
Source: CSO, RBI, CEIC, MOFSL

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