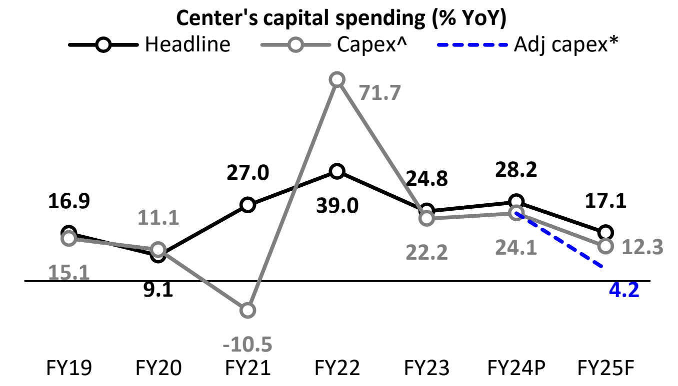
Decoding the capex budget!

Combined capex likely to rise to 3.7% of GDP in FY25BE

- **Once again, the Government of India (GoI) sent a very loud and clear message with the Union Budget 2024-25 that its priority is to focus on the long-term macroeconomic stability, even if it means sacrificing growth for the short term. We have highlighted the restricted ability of the GoI to support economic growth if it is serious about its fiscal deficit consolidation path. However, like every year, more time needs to be spent to understand the nuances of the capex budget.**
- **The GoI has not only prioritized the deficit consolidation path, but also continued to focus on improving the quality of expenditure by raising its total capital spending by 17.1% YoY to INR11.1t in FY25BE (unchanged from the Interim Budget 2024 presented in Feb'24), up 3.3x in just five years from INR3.4t in FY20. If achieved, the GoI's capital spending would jump to 3.4% of GDP in FY25BE from 1.7% of GDP during the pre-Covid period (FY18-FY20).**
- **However, two-three important adjustments are needed to understand the true extent of the GoI's investment push: 1) Capital spending has two parts – capital outlays/expenditure (or capex) and loans and advances (L&As). The GoI has budgeted INR1.6t of capital spending as L&As to states (vs. INR1.4t in FY25[I]). 2) The GoI has included equity infusion of INR829b to BSNL in FY25BE under capex (same as in FY25[I]), and 3) there is a new entry totaling INR626b called 'New Schemes' under the Ministry of Finance, for which we could not find any details (vs. INR704b in FY25[I]). After adjusting for the first two adjustments, GoI's capex is budgeted to grow 12.3% YoY. The growth will ease to 4.2% in FY25BE, if we exclude the allocation to 'New schemes'.**
- **Further, the capex of Central Public Sector Enterprises (CPSEs), excluding the Department of Food & Public Distribution (DF&PD), must also be included to estimate the GoI's true investment plan. After four consecutive declines, CPSEs' capex is budgeted to grow 12.5% YoY this year (better than 2.4% growth budgeted in FY25[I]), led by HUDCO.**
- **Overall, the combined capex (of the Center and CPSEs) is budgeted to grow 12.4% this year (or just 6.5% if we exclude INR626b as 'New Schemes') similar to 12.7% YoY growth in FY24P. It also means that the combined capex is budgeted at 3.7% (or 3.5%) of GDP in FY25, better than 3.6% in FY24P but lower than 3.9% of GDP in the pre-Covid years.**

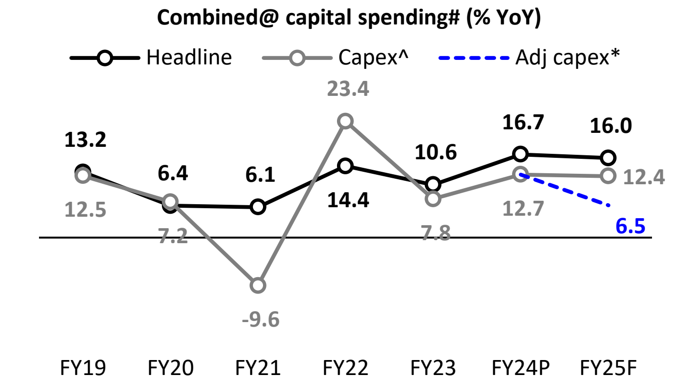
The GoI continued to focus on improving the quality of expenditure by raising its total capital spending by 17.1% YoY to INR11.1t in FY25BE, up 3.3x in the last five years. If achieved, the GoI's capital spending would jump to 3.4% of GDP in FY25BE from 1.7% of GDP during the pre-Covid period (FY18-FY20).

Exhibit 1: Center's capex budgeted to grow 4-12% YoY in FY25BE…



^Excluding Loans & advances to states and capital infusion into PSUs
*Excluding 'New Schemes' under the Ministry of Finance

Exhibit 2: …and the combined capex, with CPSEs#, is targeted to grow 7-12%



#CPSEs capex excluding DF&PD
@Center + CPSEs
Source: Budget documents, MOFSL

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What is the Center's true capex budgeted for FY25BE? After growing at an average of 30% during the past four years (FY21-FY24P), the GoI's total capital spending is budgeted to increase by 17.1% YoY this year, double of 8.5% growth budgeted in the GoI's total spending. Thus, capital spending is budgeted to rise to a two-decade high of 23% of total spending in FY25BE, almost double of 12% in FY21. Nevertheless, two-three adjustments need to be made to extract true investments of the GoI, from the reported capital spending allocation. Let's discuss them one by one.

a. **Segregate capital outlays (investments) from L&As:** A detailed ministry-wise capital spending by the GoI has two components – capex and L&As. From an average of ~10% in the pre-pandemic years, L&As accounted for ~17% of GoI's total capital spending in FY24 and budgeted at 17.3% in FY25.

Excluding L&As to states, the GoI's capex is budgeted at INR9.5t in FY25BE, up 15% YoY, following an average growth of 26% during FY21-FY24P

The GoI has budgeted L&A worth INR1.9t, including a transfer of INR1.6t to states (revised from INR1.4t in FY25[I]). These L&As will be eventually counted as states' capex, and thus, they must be excluded from the GoI's capex. Excluding L&As to states, the GoI's capex is budgeted at INR9.5t in FY25BE, up 15% YoY, following an average growth of 26% during FY21-FY24P.

Exhibit 3: Detailed analysis of capital outlays by CG and CPSEs

INR b, unless otherwise mentioned	FY22	FY23	FY24P	FY25 (I)	FY25BE
Central government capital spending (Budgeted allocation)					
Ministry of Defense	**1,380**	**1,429**	**1,543**	**1,720**	**1,720**
Ministry of Railways	**1,173**	**1,593**	**2,426**	**2,520**	**2,520**
Ministry of Road Transport & Highways	**1,168**	**2,060**	**2,639**	**2,722**	**2,722**
Department of Telecommunications	**39**	**556**[1]	**594**	**844**	**844**
Capital infusion to BSNL	0	264	550	829	829
Ministry of Civil Aviation	**624**[2]	**1**	**8**	**0**	**1**
Others	**960**	**609**	**665**	**1,589**	**1,380**[3]
Loans and advances (L&As)	**584**	**1,153**	**1,611**	**1,715**	**1,924**
States/UTs/foreign governments	225	927	1,229	1,424	1,624
Total capital spending	**5,928**	**7,400**	**9,485**	**11,111**	**11,111**
Capital outlays (Capex)[4]	5,079	6,207	7,706	8,856	8,656
Central Public Sector Enterprises (CPSEs)[5]					
Ministry of Defense	29	28	29	28	33
Ministry of Railways	734	447	200	130	130
Ministry of Road Transport & Highways	652	0	0	0	0
Ministry of Power	481	574	591	673	667
Ministry of Petroleum & Natural Gas	1,067	1,190	1,123	1,185	1,185
Ministry of Housing & Urban development	100	165	168	160	425
Others	705	922	927	934	977
Total capital outlays (Capex)[6]	**3,767**	**3,326**	**3,037**	**3,110**	**3,417**
Department of Food & Public Distribution	609	309	230	326	276
Combined capital outlays (Capex)					
Ministry of Defense	1,408	1,457	1,571	1,748	1,753
Ministry of Railways	1,907	2,040	2,626	2,650	2,650
Ministry of Road Transport & Highways	1,819	2,060	2,639	2,722	2,722
Combined capital outlays **(as a percentage of GDP)**	**8,846** **(3.7)**	**9,534** **(3.5)**	**10,744** **(3.6)**	**11,967** **(3.7)**	**12,073** **(3.7)**
YoY (%)	**23.4**	**7.8**	**12.7**	**11.5**	**12.4**

[1]Includes transfer of INR265b to universal service obligation fund

[2]Includes INR624b on account of equity infusion to AIAHL

[3]Includes INR626b as 'New Schemes' under the Ministry of Finance

[4]Excluding capital infusion into PSUs and L&As to States

[5]FY24REs since FY24P not available

[6]Excluding DF&PD, primarily Food Corporation of India (FCI)

Source: Union Budget documents, MOFSL

b. **Equity infusion into PSUs must also be excluded:** A detailed ministry-wise analysis of the capex also reveals the following:
   i. More than a third of the rise in the GoI's capex (excluding L&As to states) in FY22 was on account of the equity infusion into Air India Assets Holding Ltd. This was the primary reason why the GoI's capital spending surpassed INR1.1t in Dec'21 – the highest ever in a single month. We have excluded this amount from FY22 to estimate the true GoI capex.
   ii. Further, the Department of Telecommunications (DoT) has included financial relief/capital infusion totaling INR164b to BSNL in FY23 (down from INR447b/INR333b in FY23BE/FY23RE), INR648b in FY24RE (down from INR529b in FY24BE) and another INR829b in FY25BE. Thus, a total of INR1.74t has been allocated during the past three years as capital infusion into BSNL under the GoI's capital spending. Based on provisional monthly data, capital expenditure under DoT amounted to INR594b in FY24, because of which we have assumed BSNL capital infusion of INR550b. These capital infusions pushed the allocation under the Ministry of Communications from less than INR40b in FY22 to INR844b in FY25BE.

A total of INR1.74t has been allocated during the past three years as capital infusion into BSNL under the GoI's capital spending

After excluding L&As to states and such financial support to various PSUs, the GoI's capex is budgeted to rise 12.3% YoY in FY25BE

After excluding L&As to states and such financial support to various PSUs, the GoI's capex is budgeted at INR8.7t, up 12.3% YoY in FY25BE, following an average growth of 23.6% during FY21-FY24P *(Exhibit 3 on the preceding page)*.

c. **'New Schemes' under the Ministry of Finance:** Finally, the details of the GoI's capital spending reveal that the allocation under 'other general economic services' is budgeted at INR633b in FY25 (INR711b in FY25[I]), up from INR5b in FY24RE (and even lower in the previous years). When we dug deeper, we found that the GoI has allocated a sum of INR626b as 'New Schemes' under other expenditure in the Department of Economic Affairs, Ministry of Finance.

   Unfortunately, we could not find any further details regarding 'New Schemes', just like in the Interim Budget. We understand that this amount could be allocated against some schemes that are work-in-progress. It is possible that this amount is against some schemes announced by the FM during the Budget speech, and as the details are worked out, the allocations would be sanctioned to the respective ministries/departments. We are not sure if our understanding is correct, and thus, not confident about the potential multiplier impact of this spending. It is, therefore, not clear if this sum of INR626b (included under Others in *Exhibit 3* above) should be a part of the Center's capex or not.

If we further exclude INR626b under 'New schemes', the GoI's adjusted capex is budgeted to grow only 4.2% YoY this year

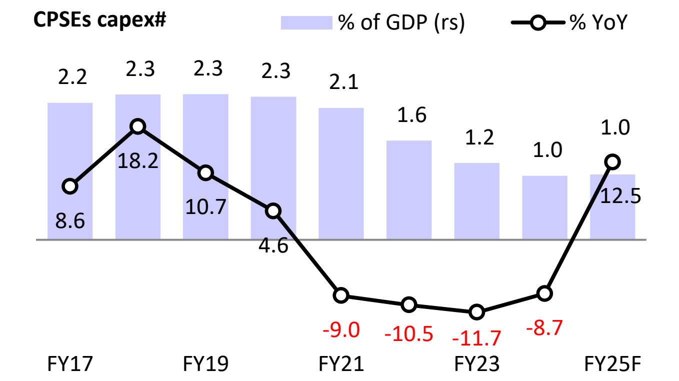
If we do not exclude 'New schemes', the GoI's capex is budgeted to grow 12.3% YoY in FY25BE, slower than in the previous years, but still a reasonably decent growth considering its commitment to deficit consolidation. However, if we further exclude INR626b, the GoI's adjusted capex is budgeted to grow only 4.2% YoY this year, significantly slower than in previous years *(please see Exhibit 1)*.

Internal and Extra Budgetary Resources (IEBR) of CPSEs also budgeted to grow after four years of contractions: Budget allocations only account for a portion of the total capital spending by the GoI. The planned capital outlays (or capex) by CPSEs, and their likely financing, are also provided for in the Union Budget. From an economic perspective, what matters are the combined capital outlays of the GoI and CPSEs.

Excluding DF&PD, IEBR of CPSEs is budgeted to increase 12.5% YoY in FY25BE, better than 2.4% growth budgeted in FY25[I], led by HUDCO

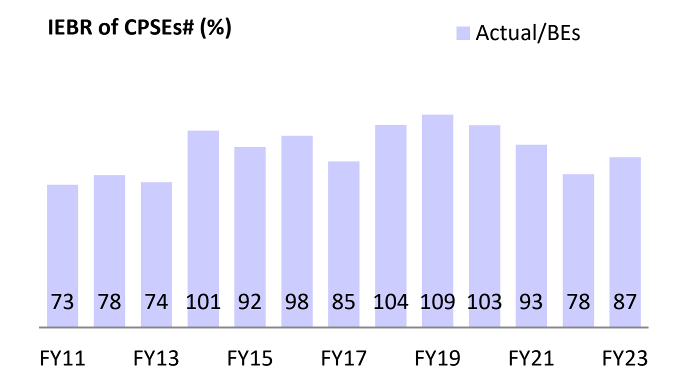
After making the above-mentioned adjustments in the GoI's investment spending, we have made one adjustment in CPSEs' capex. Since FY18, the DF&PD (which includes the allocation to FCI) has undertaken the maximum capital outlays among CPSEs, averaging to about INR2t each year during FY18-FY20. As the GoI cleared all the arrears in FY21 and took over FCI debt on its books, the off-budget capex by the DF&PD reduced to about INR600b in the following two years, i.e., FY21-FY22, before falling further to INR200-300b in the last three years (FY23-FY25BE). This, we believe, must be excluded from the aggregate IEBR of CPSEs to understand the true extent of the infrastructure push by the GoI. Accordingly, we look at the IEBR's capex, excluding DF&PD.

Exhibit 4: CPSEs capex (ex DF&PD) is budgeted to increase 12.5% YoY in FY25BE, after four successive declines



FY24RE and FY25BE #Excluding DF&PD

Exhibit 5: Actual CPSEs capex has been mostly lower than the budgeted allocation



Source: Budget documents, CSO, MOFSL

Excluding DF&PD, IEBR of CPSEs is budgeted to increase 12.5% YoY in FY25BE (better than 2.4% growth budgeted in FY25[I]), marking its first growth in the last five years *(Exhibit 4)*. Compared to the Interim Budget, capex by HUDCO explains the upward revision in CPSEs capex in FY25BE.

CPSEs capex (excluding DF&PD) fell to INR3.0t in FY24RE, from its peak of INR4.6t in FY20. In other words, from an average of 2.3% of GDP in the entire 2010s decade (peak of 3.3% of GDP in FY09), CPSEs capex declined continuously to just 1.0% of GDP in FY24RE – the lowest in at least the past two decades. It is budgeted to remain unchanged at 1.0% of GDP in FY25BE.

Actual capex by CPSEs tends to be 90-95% of BEs/REs, with much sharper cuts vs. BEs in FY22 and FY23

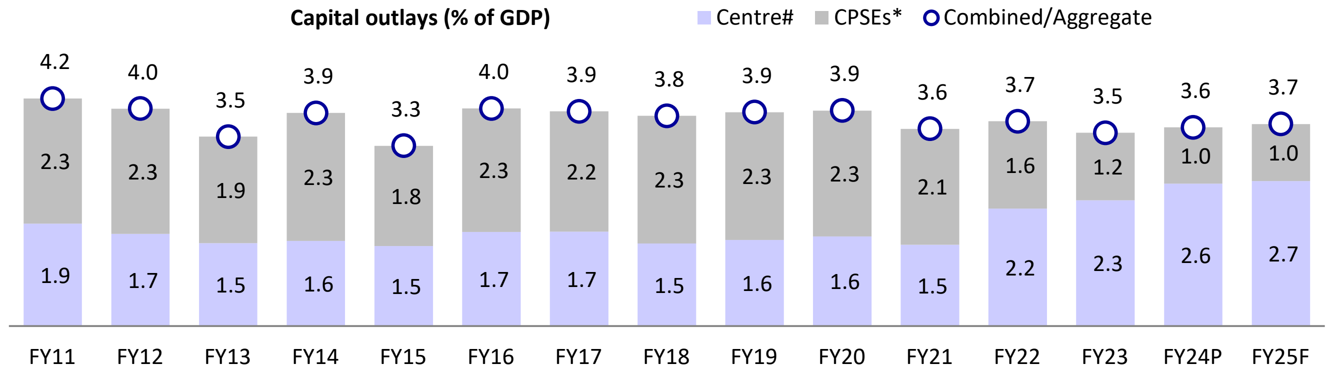
At the same time, historical data suggests actual capex by CPSEs tends to be about 90-95% of the budgeted and revised estimates (BEs/REs), with much sharper cuts vs. BEs in FY22 and FY23 *(Exhibit 5)*. CPSEs' capex was revised down to INR3t in FY24RE, from INR3.4t in FY24BE, and thus, FY25BEs could also be revised.

Combined capex budgeted at 3.7% of GDP in FY25 vs. 3.6% in FY24RE, but lower than 3.9% of GDP in the pre-Covid period: Overall, from an economic perspective, what matters is the combined capex of the GoI (on-budget) and IEBRs of CPSEs (off-budget). With various adjustments (excluding L&As to states, capital infusion to PSUs and DF&PD from CPSEs), our estimates suggest that the combined capital outlays grew 12.7% YoY in FY24P and were budgeted to rise by 12.4% YoY in FY25 *(Please see Exhibit 2 above)*.

The combined capex (of the Center and CPSEs) is budgeted at 3.7% of GDP in FY25 vs. 3.6% in FY24RE, but still lower than 3.9% of GDP in the pre-Covid period

Effectively, a large part of the increase in the GoI's capex (excluding L&As) to 2.7% of GDP in FY25BE from 1.6% of GDP in FY20 is offset by lower budgeted capex by CPSEs at 1.0% of GDP from 2.3% during the corresponding period. The Center's higher capex is, therefore, a reallocation of the off-budget capex, rather than additional spending. Accordingly, the combined capex (of the Center and CPSEs) is budgeted at 3.7% of GDP in FY25 vs. 3.6% in FY24RE, but still lower than 3.9% of GDP in the pre-Covid period *(Exhibit 6)*.

Exhibit 6: Combined capital outlays of the government and CPSEs



#Excluding L&As to states and equity infusion to PSUs
*Excluding DF&PD
Source: Union Budget documents, CSO, MOFSL

After adjusting the Center's capex by INR626b allocated as 'New schemes', the combined capex will fall to 3.5% of GDP this year

After adjusting the Center's capex by INR626b allocated as 'New Schemes' under the Ministry of Finance, the Center's capex growth will decelerate to just 4.2% and the combined capex growth will be only 6.5% YoY in FY25BE, instead of 12.4% YoY without this adjustment *(please see Exhibit 2 above)*. Accordingly, the combined capex will fall to 3.5% of GDP this year.

Defense is budgeted to grow decently, with much weaker growth in railways and road transport & highways: Three sectors – roads, railways and defense – account for about four-fifths of the total capex by the center. However, the Ministry of Road Transport & Highways (MoRTH), Ministry of Railways (MoR) and the Ministry of Defense (MoD) also incur capex on their own accounts, shown as off-budget spending under IEBR of CPSEs. It is important to understand that while the Center has been showing strong capex growth in these areas in the last few years, what matters is the combined capex (on-budget and off-budget) in these areas, including spending by the these ministries outside the budget allocation.

As shown earlier, in order to improve transparency and to provide relief to the National Highways Authority of India (NHAI), the GoI had decided to include NHAI's borrowings in its own books in FY23, reducing it to nil by CPSEs from INR652b in FY22 *(Exhibit 3 above)*. Consequently, while the Center showed a massive 76% YoY rise in capex of the MoRTH in FY23, the combined capex of the MoRTH grew 13.2%

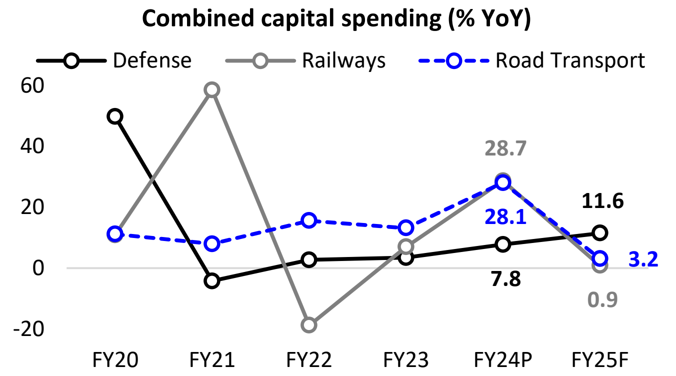
YoY in FY23. The growth in the combined capex on the roads sector is estimated to grow 28.3% in FY24P, before falling sharply to just 3.2% YoY in FY25BE *(Exhibit 7)*.

In FY25, the capex growth in the roads & railways sector is budgeted at just 1-3%, from 28-29% YoY in FY24P

Similarly, while the GoI's capex of the MoR grew 36% YoY in FY23 and a strong 52% YoY growth in FY24P, the combined capex in the Railways increased by only 7% YoY in FY23 and 28.7% YoY in FY24P. This was because of the massive reduction in CPSEs capex *(Exhibit 3 above)*. With almost negligible capex planned by the MoR, the combined capex of the MoR is budgeted to grow by just 0.9% YoY in FY25BE *(Exhibit 7)*.

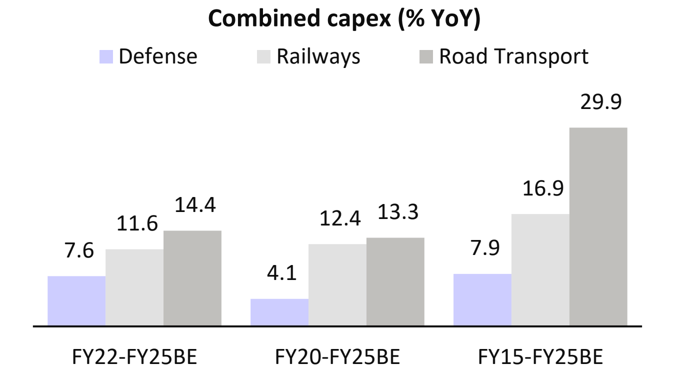
Further, the combined capex in the defense sector is budgeted to grow 11.6% YoY in FY25BE, the highest in five years and compared to 7.8% YoY in FY24P.

Exhibit 7: Capex by 'Railways' and 'Roads & Highways' budgeted at just 1-3% next year…



Including Center and CPSEs

Exhibit 8: …but the 3-yr, 5-yr and 10-yr CAGR in these areas is considerably strong



Source: Budget documents, MOFSL

Over the past five (and ten) years, the CAGR in the railways/roads capex stands at 13.3%/12.4% (29.9%/16.9%)

Although the annual growth in the roads & railways sector is budgeted at a muted pace in FY25BE, a look at the CAGR confirms a strong bias of the GoI toward its capex commitment *(Exhibit 8)*. Over the past five (and ten) years, the CAGR in the railways/roads capex stands at 13.3%/12.4% (29.9%/16.9%). **The long-term average growth in the defense sector, however, is more modest, and thus, we expect the GoI to focus more on this area in the coming years**.

Overall, just like during the **Interim Budget 2024-25**, the GoI has rightly prioritized the long-term macroeconomic stability, even if it implies sacrificing growth for the short run. Accordingly, although the capex growth has also weakened in FY25BE (especially in the roads and railways sector), it has grown at a strong pace over the past five or ten years (click here for further details).

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