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Professional Risk Opinion

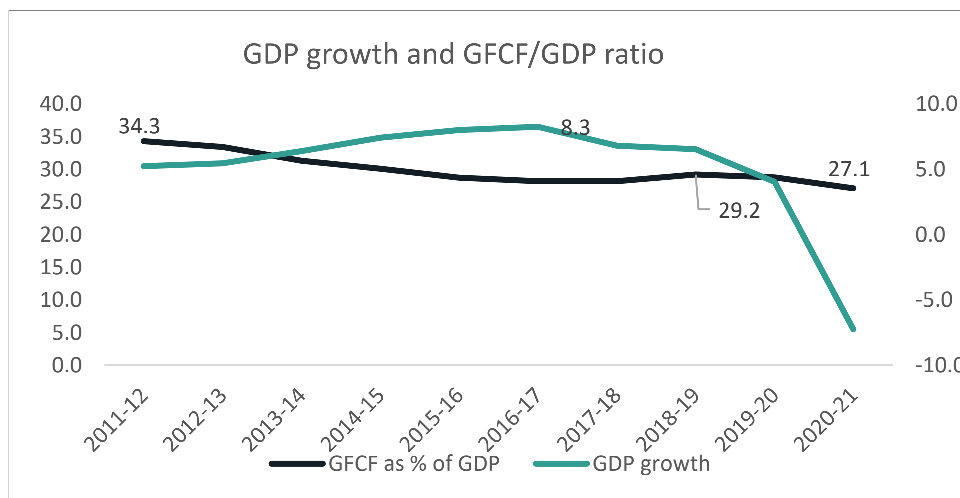
Deleveraging in India Inc.

September 06, 2021 I Economics

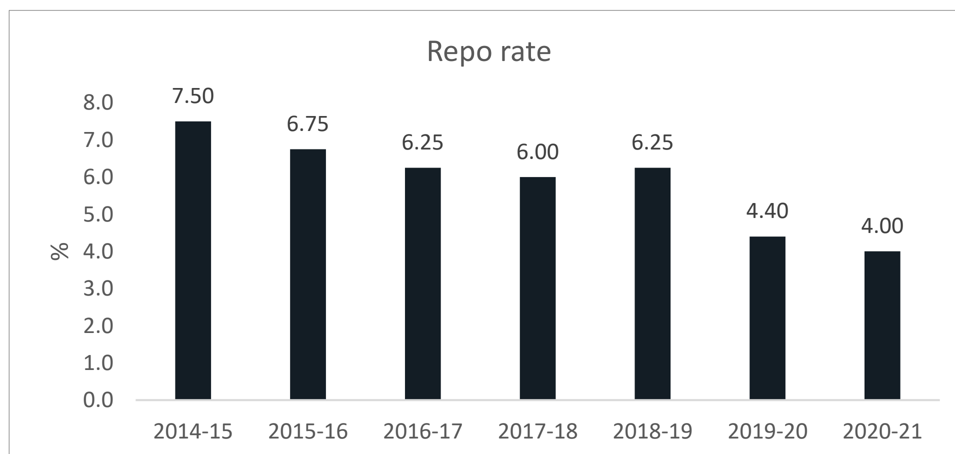
One of the fallouts of the pandemic was the phenomenon of deleveraging in the corporate sector. This was not really surprising as investment activity slowed down and the future was laden with uncertainty. This was observed in almost all sectors in FY21 as a sample of 794 companies which have published their balance sheets for this year reveal. When the finance companies are excluded, the sample of 691 companies show a sharper fall in outstanding debt. In the last 5 years ending FY21, growth in total outstanding debt was CAGR of 9.2% for the larger sample which comes down to 5% for the sample excluding finance companies.

Overall, the debt for the 691 companies increased from Rs 9.47 lakh crore in FY17 to Rs 11.50 lakh crore in FY21. However, in this period it had declined in FY18 to Rs 9.37lakh crore and once again in FY21 from Rs 12.81 lakh crore in FY20. In FY19 debt was Rs 10.41 lakh crore. Clearly the tendency to deleverage is not just a pandemic situation but a policy that has been followed post the AQR process when banks came under pressure due to the ballooning of the NPAs.

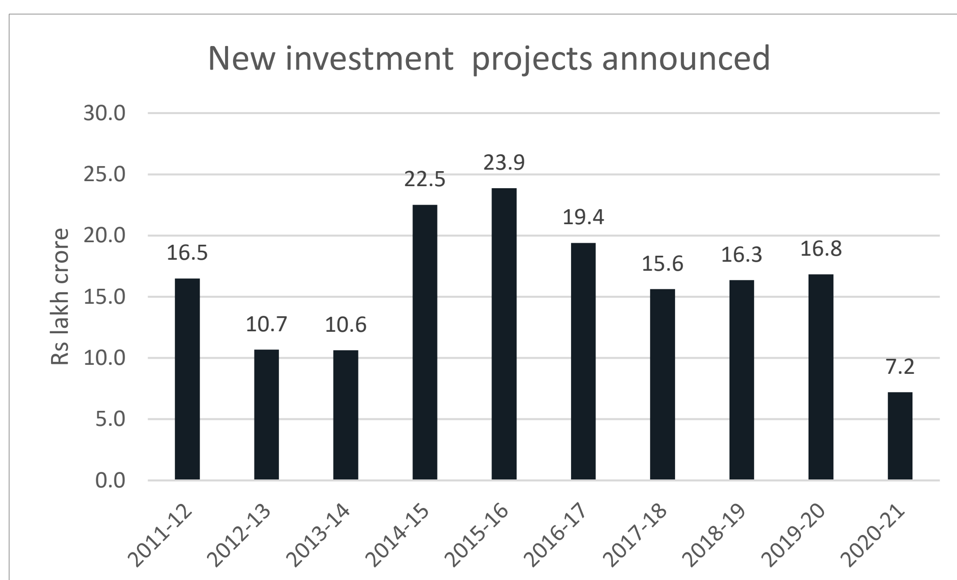
The overall investment scenario in the country has been typified by a decline in the gross fixed capital formation rate. This also matched the declining trend in GDP growth rate after 2017-18 when it peaked at 8.3%. Capital formation was also on a downward path in an analogous manner. In the last 9 years there was a continuous decline in the capital formation rate with only one year, 2018-19 witnessing an increase from 28.2% to 28.9%. It is now at 27.1%.



A combination of rising NPAs as well a stagnant economic growth path which tended to decline contributed to the deleveraging process. This is notwithstanding the fact that the central bank has been working to lower the overall lending rates by reducing the repo rate.



Simultaneously there was a decline in the volume of new projects announced in the last few years as indicated by the graph below based on date from CMIE.

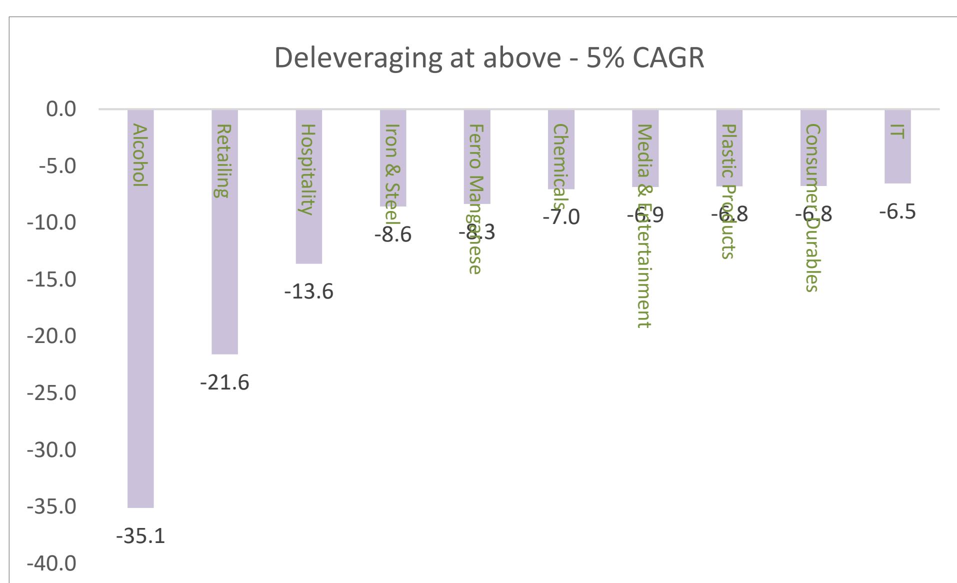


Source: CMIE

The uncertainty of future cash flows and the banking environment have both combined to make companies seriously look at this option. At times companies have gone in for refinance to manage their costs but repaying debt has become common in these economic slowdowns. Several large to medium companies are in the process of going through with the insolvency proceedings and hence have looked at repaying debt when possible, rather than borrowing more.

Where has sharp deleveraging taken place?

Of the 34 non-BFSI industries, 21 have witnessed a fall in CAGR of outstanding debt by FY21.



Some of these industries have been hit by the lockdown such as retailing, iron and steel, hospitality, media, consumer durables due to demand conditions being low. IT would be a conscious decision as this sector has been doing well. But the debt level is just 0.6% of total and hence is insignificant. In fact, among these borrowers, the only big ticket is iron and steel with share of 9.1%. clearly this industry is confronted by volatile demand as well as the pending cases at the IBC.

CAGR of o/s debt for top 10 industries with high share in total debt

	CAGR (%) 2017-21	Share in total debt (%)
Crude Oil	18.7	34.1
Telecom	11.9	10.7
Iron & Steel	-8.6	9.1
Non - Ferrous Metals	-4.1	5.8
Automobile & Ancillaries	6.3	5.4
Power	-2.2	5.0
Healthcare	-1.5	4.0
Logistics	7.7	3.7
Infrastructure	9.1	3.6
Construction Material	11.0	2.8

The top industries which account for around 84% of total outstanding debt in 2021 had witnessed 4 of them deleveraging during this period. These are iron and steel, non-ferrous metals, power and healthcare. These sectors interestingly were at the lower level of the NPA spectrum. As of March 2021 the sector-wise NPAs read as follows: gems and jewelry 24%, construction 23.5%, engineering 18%, mining 16.1%, food processing 13.5%, textiles 12.3%, infra 11.5%, power 9.3%, metals (10.9%), and auto (7%) as per RBI's FSR.

In FY21, 21 of the 34 industries in the sample had witnessed a decline in o/s debt. 357 companies lowered their debt while another 144 had virtually unchanged levels. The lockdown had made companies more conscious of their debt levels notwithstanding the concessions given like moratorium and restructuring by the RBI. It may be pointed out that the low interest rate regime and surplus liquidity in the system did not cause companies to borrow more and in fact made them more conscious of their debt levels. Several companies used their surpluses to repay costly debt. Plans for expansion were kept on hold which meant that additional borrowing was restricted to financing working capital requirements.

The act of deleveraging though good at the micro level does not bode well for the investment cycle as it means that there is less appetite for taking calls on capital. Further when companies either use their cash surpluses to repay debt or go in for asset sales for this purpose, it does send a signal of business pessimism. Putting both these factors together it could signal weakness in future growth prospects for the sector.

At the consumer end, industries like textiles, agricultural products, hospitality, media, paper and durables have witnessed negative CAGR. Ideally with consumerism picking up, one would expect these industries to expand. Partly, due to the pandemic and the low growth tendencies even before March 2020, these industries have been more cautious on the borrowing side. The industries related finally to infra like metals and power could be linked with investment projections which do not look robust for this sample as of March 2021.

(the details of debt, compound growth and share int total debt is given in the Appendix)

Concluding remarks

There has been a slowdown in growth in debt of India Inc in the last few years. This is due to a combination of several factors like low economic growth, fewer investment projects, legacy issue of NPAs with the result of several companies being under the ambit of IBC. Against this environment, even though interest rates have been brought down considerably by the central bank, companies have been using their surpluses to repay debt at times. This has been exacerbated by the pandemic which has caused companies to retire debt in uncertain times. The recent flurry of equity issuances can be a way out at the margin for some companies to finance future growth outside the debt circle. Deleveraging at a time when the economy is on a low-growth path is not a very cheerful sign as it does point to caution and to an extent risk aversion in some sectors.

Appendix: Outstanding debt of various sectors and CAGR 2017-21

Rs crore	FY17	FY21	CAGR (%)	Share in FY21 (%)
All companies	9,47,423	11,50,786	5.0	100.0
Crude Oil	1,97,591	3,92,336	18.7	34.1
Telecom	78,309	1,22,655	11.9	10.7
Iron & Steel	1,50,442	1,05,146	-8.6	9.1
Non - Ferrous Metals	79,202	67,040	-4.1	5.8
Automobile & Ancillaries	48,725	62,168	6.3	5.4
Power	62,720	57,381	-2.2	5.0
Healthcare	48,562	45,764	-1.5	4.0
Logistics	31,413	42,248	7.7	3.7
Infrastructure	29,255	41,388	9.1	3.6
Construction Materials	21,548	32,704	11.0	2.8
Realty	31,064	32,502	1.1	2.8
Chemicals	24,632	18,395	-7.0	1.6
Agri	19,254	17,598	-2.2	1.5
Textile	16,965	16,353	-0.9	1.4
Capital Goods	11,745	14,840	6.0	1.3
Trading	16,762	14,386	-3.7	1.3
Diversified	15,472	13,425	-3.5	1.2
IT	8,699	6,637	-6.5	0.6
FMCG	4,055	6,251	11.4	0.5
Inds. Gases & Fuels	5,063	5,991	4.3	0.5
Hospitality	9,636	5,367	-13.6	0.5
Diamond & Jewellery	2,218	4,629	20.2	0.4
Media & Entertainment	5,239	3,944	-6.9	0.3
Paper	4,002	3,635	-2.4	0.3
Electricals	2,955	2,979	0.2	0.3
Aviation	2,596	2,506	-0.9	0.2
Miscellaneous	2,651	2,499	-1.5	0.2
Consumer Durables	3,036	2,294	-6.8	0.2
Insurance	485	2,285	47.3	0.2
Retailing	4,624	1,748	-21.6	0.2
Plastic Products	2,216	1,673	-6.8	0.1
Alcohol	4,666	827	-35.1	0.1
Ferro Manganese	941	664	-8.3	0.1
Gas Transmission	549	488	-2.9	0.0

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