Where is investment taking place?

Contact:

Economics and Industry Research
91-022-6754 3489

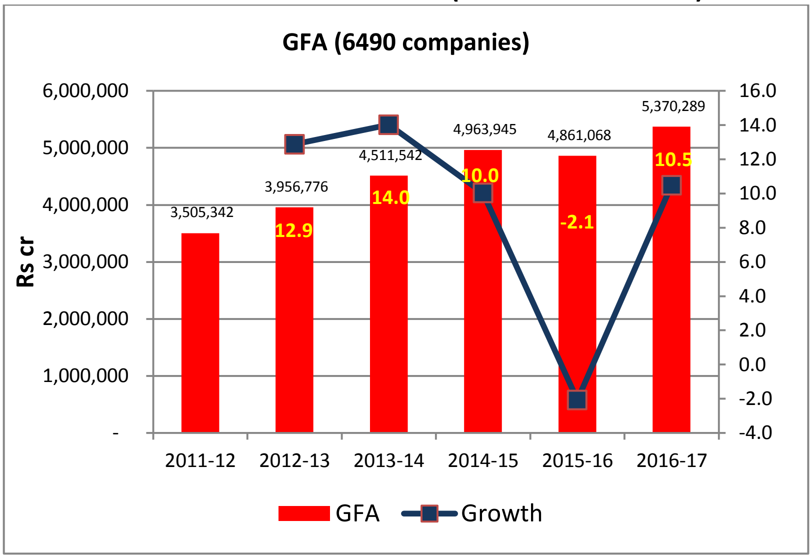
Mradul Mishra (Media Contact)
mradul.mishra@careratings.com
91-022-6754 3515

One of the major challenges for the economy is investment which is guided by both demand and supply side forces. A concern is that the gross fixed capital formation (GFCF) rate has been coming down in recent years. For the economy as a whole it has come down from 34.3% in FY12 to 28.5% in FY18, and has remained unchanged in the last couple of years. Quite clearly the level has to be increased to above 30% to bring about accelerated growth in the economy.

The foregoing analysis looks at the aspect of gross fixed assets for a set of 6,490 companies since FY12. The idea is to ascertain the leading sectors in terms of size of gross fixed assets (including capital work in progress) and identify the high growth areas. This is done for both the absolute level of gross fixed assets and incremental assets which would correspond with what is happening at the national level. The time period chosen for this exercise is 2011-12 to 2016-17.

The Chart below shows that aggregate GFA for this sample of companies increased at a CAGR of 8.9% from Rs 35.05 lkh crore to Rs 53.70 lkh crore during the five-year period. The growth rate however was uneven over the years, where it declined in 2014-15 and 2015-16 before increasing in 2016-17.

Chart 1: Gross fixed assets (2011-12 to 2016-17)



Source: ACE Equity

Table 1 below identifies some of the leading sectors in terms of size of GFA in 2016-17 where the share is more than 1% in total.

As can be seen, the top 5 sectors accounted for around 62% of total GFA of the entire sample. Crude oil, power, iron & steel, telecom and banks were the main industries which topped the chart. In case of banks the size would be dependent on the investment in IT and property.

The next set of 5 industries had a share of 20% and included infrastructure, auto, non-ferrous, chemicals and IT.

Table 1: Shares of leading industries in GFA (Rs cr)

	2016-17	Share (%)
Total	**5,168,622**	**100.0**
Crude Oil	979,273	18.9
Power	906,416	17.5
Iron & Steel	600,138	11.6
Telecom	639,420	8.9
Bank	230,735	4.5
Infrastructure	227,325	4.4
Automobile & Ancil	205,439	4.0
Non - Ferrous Metals	186,809	3.6
Chemicals	133,503	2.6
IT	120,143	5.8
Construction Materials	109,432	2.1
Textile	104,202	2.0
Logistics	85,424	1.7
Capital Goods	64,522	1.2
FMCG	64,448	1.2
Mining	63,004	1.2
Inds. Gases & Fuels	62,647	1.2

Table 2 provides a view on the CAGR in GFA of different sectors in the last 5 years. Here the picture is different from Table 1 with IT, healthcare, banks, retailing, and ship building witnessing the highest growth rates.

Table 2: Compound growth in GFA (2011-12 to 2016-17)

Industry	%	Industry		Industry	%
Healthcare	24.5	Trading	9.1	Capital Goods	3.8
IT	17.6	Aviation	8.8	Const Material	3.6
Bank	17.1	FMCG	8.4	Mining	3.6
Telecom	16.5	Infrastructure	7.8	Chemicals	3.2
Retailing	16.0	Auto & Ancillaries	7.4	Textile	2.9
Ship Building	15.2	Plastic Products	7.1	Agri	2.6
Finance	12.8	Alcohol	6.9	Inds. Gases & Fuels	2.5
Non - ferrous Metals	12.2	Insurance	6.7	Hospitality	2.0
Diamond, Jewellery	11.2	Paper	6.3	Ferro Manganese	1.1
Iron & Steel	10.8	Crude Oil	6.3	Abrasives	-0.8
Media, entertain	10.6	Logistics	6.1	Gas Transmission	-1.3
Education	9.7	Electricals	5.7	Realty	-1.9
Power	9.5	Consumer Durables	4.5	**All industries**	**8.9**

- 14 of the 38 sectors witnessed higher than average growth in GFA during this period.

- Higher CAGR was witnessed in case of 8 service industries like IT, banking, finance, retail, diamonds etc, media, education and trading. Their share in total GFA was however just 12.5%.
- Growth in GFA for crude oil at 6.3% was lower than the sample average, while that for power, iron & steel and telecom was higher.

Table 3 gives information on incremental investment in GFA for the last 5 years. The idea is to analyze as to which sectors have dominated in fresh investment in this time period. Total investment has been around Rs 18 lkh crore by this set of companies, of which 72% was by the top 5 industries –telecom, power, oil and steel have dominated with banks following.

Table 3: Cumulative incremental GFA: 2012-13 to 2016-17

Sector	Investment	Share	Sector	Investment	Share
Telecom	341,925	19.0	Retailing	8,190	0.5
Power	330,591	18.4	Healthcare	7,666	0.4
Crude Oil	256,178	14.2	Ind. Gases & Fuels	7,147	0.4
Iron & Steel	239,985	13.3	Trading	5,625	0.3
Bank	125,991	7.0	Paper	5,622	0.3
Non - Ferrous Metals	81,527	4.5	Agri	3,990	0.2
Infrastructure	71,045	3.9	Hospitality	3,018	0.2
IT	66,776	3.7	Alcohol	3,008	0.2
Automobile & Ancillaries	61,375	3.4	Electricals	2,793	0.2
Logistics	21,769	1.2	Insurance	2,375	0.1
FMCG	21,353	1.2	Consumer Durables	1,349	0.1
Chemicals	19,456	1.1	Ship Building	1,338	0.1
Finance	18,569	1.0	Diamonds etc.	1,257	0.1
Construction Materials	17,873	1.0	Education	413	0.0
Aviation	15,411	0.9	Ferro Manganese	229	0.0
Media & Entertainment	15,190	0.8	Abrasives	-46	0.0
Textile	13,780	0.8	Gas Transmission	-444	0.0
Capital Goods	10,867	0.6	Realty	-4,223	-0.2
Mining	10,271	0.6	**Total**	**17,99,305**	**100**
Plastic Products	10,068	0.6			

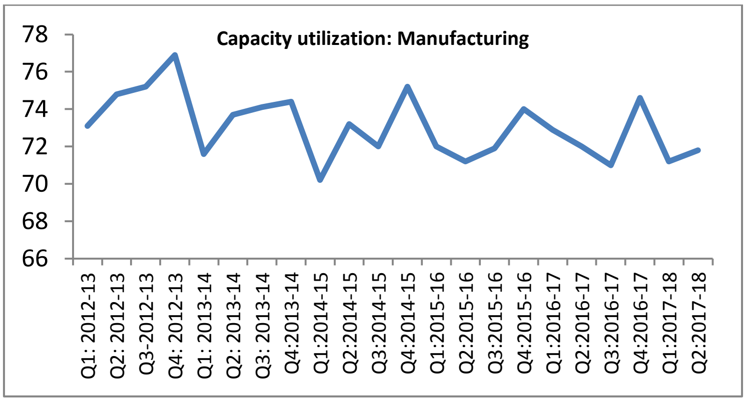
Some factors which have influenced capital expansion in various industries are tabulated below.

Sector	Factors driving expansion in assets
Telecom	Expansion of networks along with modernization of existing network infrastructure by telcos to adopt to new technologies and to acquire spectrums are believed to have resulted in higher investments.
Power	While expansion in thermal power dominated to begin with, interest increased for setting up of renewable energy.
Crude oil	Higher oil prices encouraged drilling and refinery capacity expansion. Overseas acquisition of oilfields Goal to become more self-sufficient in oil and gas has driven expansion plans.
Steel	Factors that have driven expansion include growth in construction, automotives, capital goods sectors among others and modernization/upgradation of steel plants undertaken by the companies. Also, 100% FDI allowed by the government in the steel sector has supported investments.
Non-ferrous metals	Expansion witnessed in smelting capacity in aluminum
IT	Proliferation of startups including e-commerce has widened scope for asset creation.
Automobiles	Several companies gone in for expansion New foreign players add to assets with capacity being created along with capacity addition by existing players.
FMCG	Asset creation driven more by product innovation and new players expanding in a big way
Infrastructure	Led by government spending on roads, railways and urban development
Construction material	Cement being the major constituent, a slowdown in the real estate sector caused slower capacity addition in the period 2012-17. Thrust on affordable housing to be the driver in immediate future.
Aviation	Expansion in network coverage by existing scheduled airlines and permission given to new airlines i.e. Vistara and Air Asia.
Media and entertainment	Lead by companies offering DTH/cable services
Mining	Investment linked to power sector performance.
Retail	Driven by store expansion in the organized retail segment.

Lower investment in the corporate sector can be ascribed to various sets of factors, which would also tend to be industry-specific:

1. Capacity utilization has been coming down and is in the region of around 70-72%, with spikes being witnessed in the fourth quarter of financial years. (See chart below). Fresh investment is usually considered when the utilization rate is moving up and reached the threshold of 78-80%.

Chart 1: Capacity utilization 2012-18



2. Low growth in demand which was impacted by a combination of high inflation in the period 2012-13 and 2013-14 and slowdown in income growth.
3. The legacy issues of policy impasse played its way in sectors concerning natural resources.
4. CMIE data shows that during the period 2012-13 to 2016-17 an average of Rs 11.64 lkh crore of projects have been dropped – cumulative of Rs 58.2 lkh crore. This compares with an average annual of Rs 4.5 lkh crore being dropped in the preceding five year period. (this includes abandoned, stalled and shelved projects)
5. Interest rates were argued to be high even though the repo rate came down from 8.5% in 2011-12 to 6.25% in 2016-17. The repo rate is presently 6%. The weighted average base rate of banks however came down less significantly from 10.48% to 9.5% - around 100 bps compared with 225 bps in policy rate.
6. From the perspective of banks, gross NPA ratio increased from 2.25% in 2011-12 to 9.6% in 2016-17 and further to 10.2% in September 2017. (The stressed asset ratio was 12.2%). This has also made them discreet when lending to such industries.
    a. The sectors which had high stressed assets ratio as of September 2017 were metals (44.5%), engineering (31%), mining (27.1%), construction (26.7%), infrastructure (19.6), vehicles (21%), textiles (23.7%) etc.

Concluding remarks

Increase in investment in capital will clearly be the way forward for accelerated economic growth. However, all these challenges have to be addressed. While some relating to banking would require government intervention which is already in progress, overall macroeconomic conditions have to show a turnaround which will happen gradually in the next couple of years. The regime of low interest rates may have ended as they are poised to increase or at best remain unchanged this year. Growth in demand and better capacity utilization would be the clue to higher investment in manufacturing, while the Central government can be the driver of infrastructure investment, with private investment entering in a significant manner with a lag. Higher investment in capital is more likely to be scattered and concentrated in the relatively higher growth sectors and will not be all-encompassing.

CORPORATE OFFICE:
CARE Ratings Limited
(Formerly: CREDIT ANALYSIS & RESEARCH LIMITED)
Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road,
Off Eastern Express Highway, Sion (East), Mumbai - 400 022.
Tel: +91-22-6754 3456 I Fax: +91-22-6754 3457
E-mail: care@careratings.com I Website: www.careratings.com