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Investment scenario and funding

Investment climate in India in Q1FY23 started on a weaker tone with data pointing towards sharp drop in new project announcements relative to Q4FY22. The decline was broad based but sharpest drop was visible in the manufacturing sector. However, compared with the other years, Q1FY23 announcements were higher than those in 2019, 2020 and 2021.

We have juxtaposed this picture with the major sources of funding for investment, to see whether they are also showing the same trend. Importantly, bank credit has shown a considerable pickup in Q1FY23. However, if we look at the sectoral composition, industry credit is still lagging. The major accretion in Q1FY23 has happened in the personal loan segment. However, sectoral data is only for Apr'22 and May'22, and should be read with caution. Further, within industry only chemicals and infra (especially roads and power) have seen some accretion. So the increase is not broad based within industry.

Further, if we look at the borrowing data through the debt market, it is also reflective of the fact that issuance in the corporate debt market has slowed in Q1FY23. Also 66% of issuances were by companies in the financial services space. So funding for infra projects has been minimal.

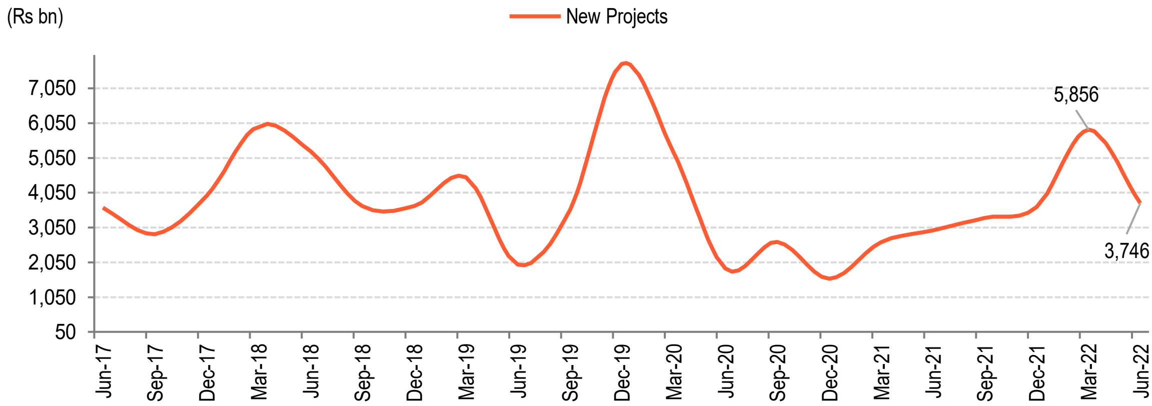
Also, through the ECB channel as well, approvals been muted in Apr'22 and May'22 compared to Q4FY22. The share of new project financing through the ECB route has been only 29%.

On the positive side, FDI has remained stable. Going forward with tightening of global and domestic financial conditions against the backdrop of a rising interest rate environment, cost of capital will go up. Elevated growth concerns might dent investor sentiments. Thus favourable business friendly policies and reduced uncertainty in policy space can comfort the business climate. The central government has announced a larger capex programme for the year which will provide the initial impetus. However, for overall capital formation to increase, private investment has to pick up at a faster pace than is happening today. This will hinge on improvement in capacity utilization across all sectors as well as interest in infrastructure which is limited today.

Investment in FY23 started on a weaker note:

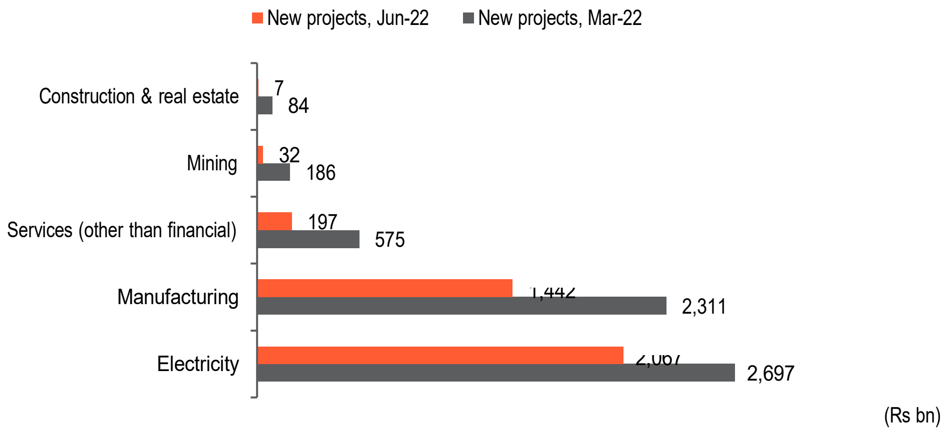
Investment scenario in India has been somber in Q1FY23 as visible in the CMIE capex data. It showed that new projects have fallen sharply from Rs 5.9tn in Q4FY22 to Rs 3.7tn in Q1FY23. The decline was broad based with most notable decline observed in the manufacturing segment where new project announcements inched down to Rs 1.4tn in Q1FY23 from Rs 2.3tn in Q4FY22. The drag down in manufacturing segment was largely led by machinery, which contributes a major share in GDP's gross fixed capital formation. However a quarterly compassion show that new project announcements this quarter were higher than those in the comparable quarter of 2019, 2020 and 2021 which is comforting.

Figure 1: New project announcements in Q1FY23 fell sharply



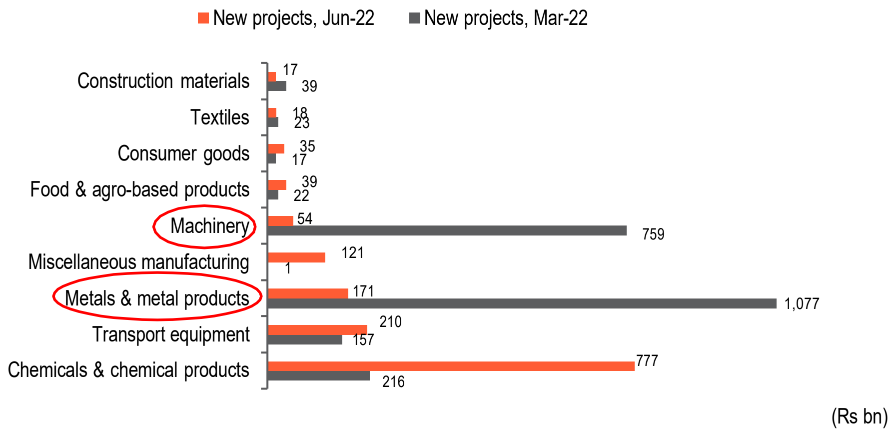
Source: CMIE, Bank of Baroda Research

Figure 2: Broad based decline in new project announcement especially in the manufacturing segment



Source: CMIE, Bank of Baroda Research

Figure 3: Metals and Machinery led the decline in the manufacturing space

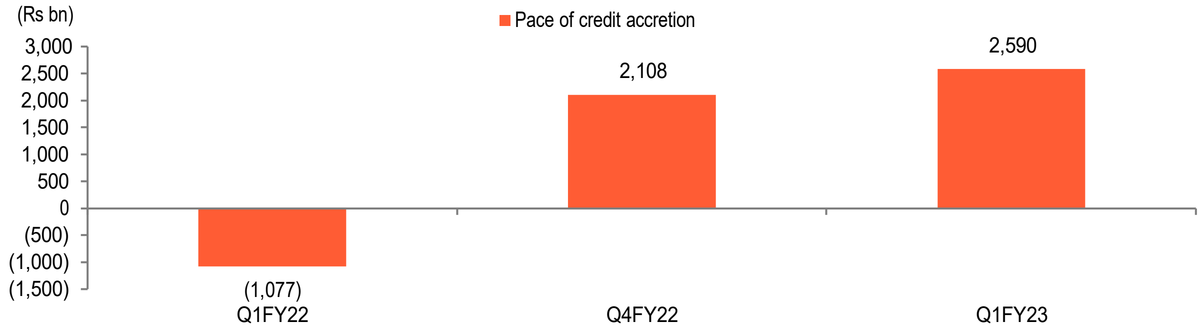


Source: CMIE, Bank of Baroda Research

How sources of funding for investment fared?

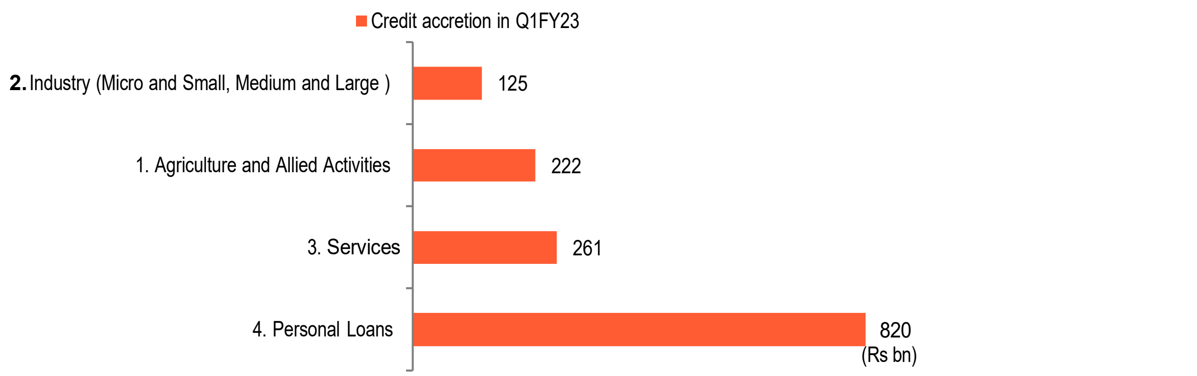
1. **Bank Credit:** Credit demand is picking pace with accretion in Q1FY23 higher at Rs 2.6tn compared to Rs 2.1tn seen in Q4FY22. In Q1FY22 incremental credit was negative. This is driven by considerable demand in the personal loan segment. However, credit accretion to industry is still happening at a slower pace. Within industry, only chemicals and infra (roads and power) has seen an accretion in credit in Q1FY23.

Figure 4: Credit accretion is happening at a faster pace in Q1FY23



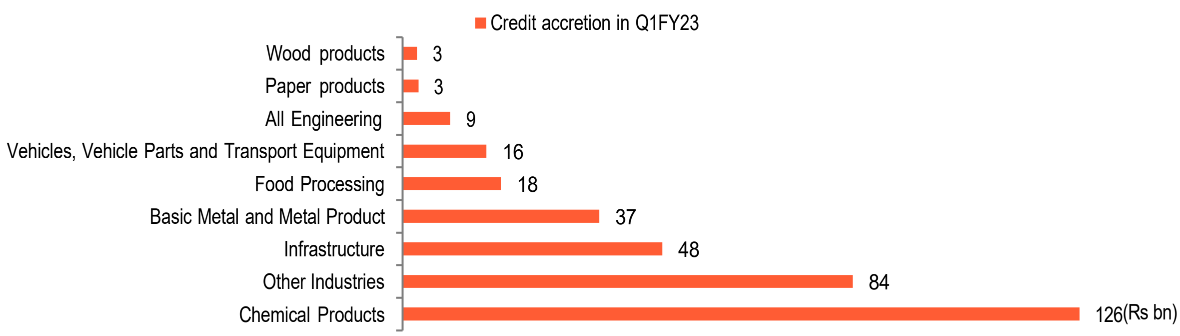
Source: CEIC, Bank of Baroda Research

Figure 5: Credit demand in the personal loan segment has been the most in Q1FY23*; industry credit demand has remained moderate



Source: CEIC, Bank of Baroda Research, Note: *Q1FY23 data pertains to Apr & May'22, thus gross bank credit in Q1FY23 will not tally

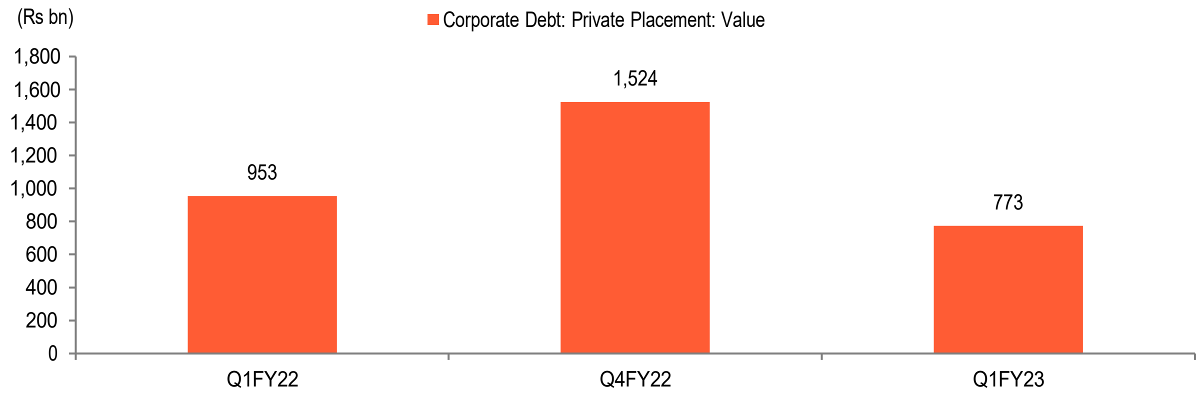
Figure 6: Within industry, only chemicals and infra has seen some momentum in Q1FY23*



Source: CEIC, Bank of Baroda Research, Note Till May'22 Note: *Q1FY23 data pertains to Apr & May'22, thus gross bank credit in Q1FY23 will not tally

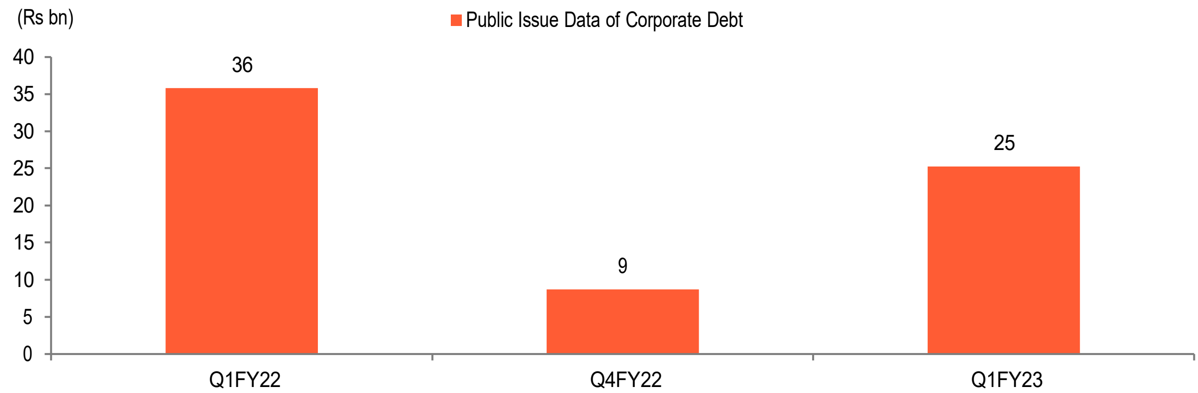
2. **Corporate Debt:** Capital raising for the purpose of investment has been muted in Q1FY23. Corporate debt through private placements, which consists of above 96% of total issuance, fell in Q1FY23 to Rs 773bn far lower compared to Rs 1.5tn raised in Q4FY22 and Rs 953 bn in Q1FY22. However, public issue of corporate debt which has a marginal share has picked up slightly in Q1FY23. Notably, majority of the issuances has been in the financial services sector (share in Jun'22). *The share of major capital intensive sector such as machinery is low at 0.2% in Jun'22.* Only shares of metals and chemical products are still comparatively better at ~8.7% in Jun'22.

Figure 7: Corporate debt issuance in Q1FY23 has gone down



Source: CEIC, Bank of Baroda Research

Figure 8: However, public issue which constitutes a small portion of overall corporate debt issuance has inched up

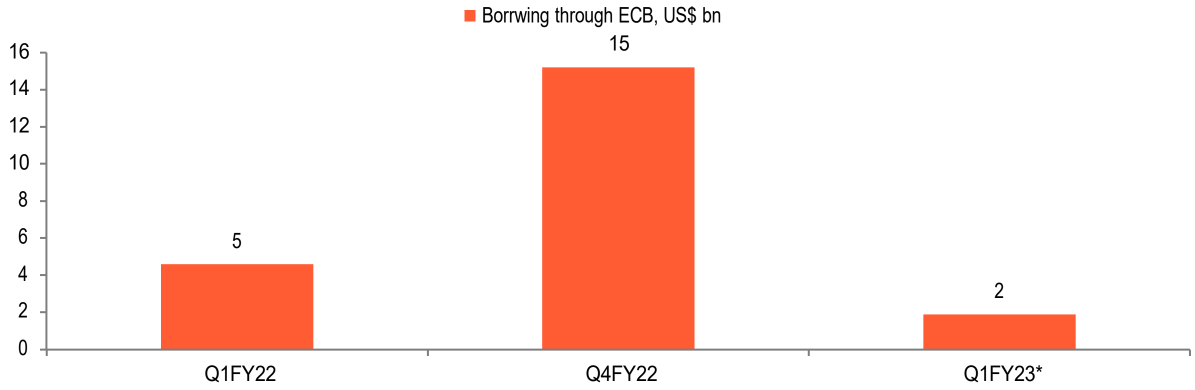


Source: SEBI, Bank of Baroda Research

3. **Foreign funding:**

   Through ECB: Borrowing through the ECB route (both automatic and approval route) has been lower at US$ 2bn in Q1FY23 (Apr & May'22) compared to US$ 15bn in the previous quarter. Even the two month's figure is lower when we compare it to the previous quarter where inflows during Jan & Feb'22 amounted to US$ 10bn. Also share of new project financing through the ECB route in May'22 was only 29%.

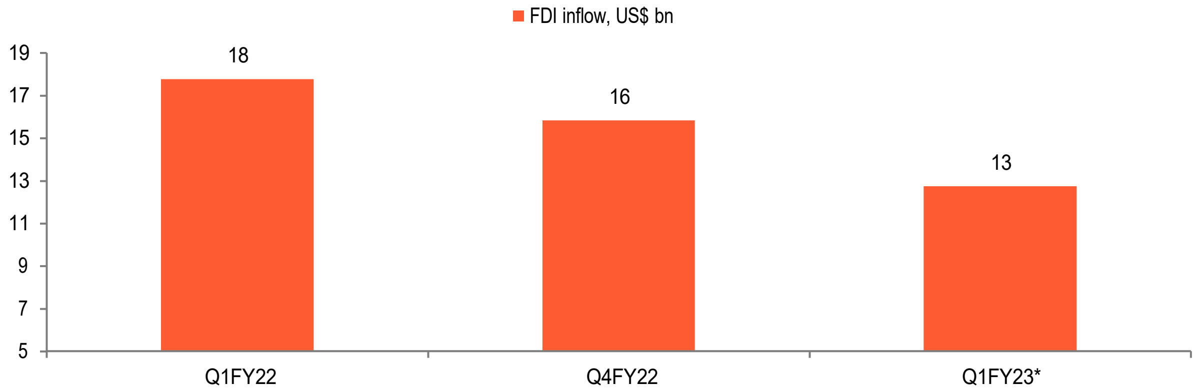
Figure 9: Borrowing through the ECB route has also moderated in the first two months of Q1FY23*



Source: SEBI, Bank of Baroda Research Note: *Q1FY23 data pertains to Apr & May'22, consists of both automatic and approval route

Through FDI: Inflow through the FDI route has been stable. The US$ 13bn inflow is for only two months (Apr & May'22), which is in line with the past two months of Q4FY22 (~US$ 11bn)., though lower than in Q1FY22.

Figure 10: FDI inflow has however remained buoyant



Source: SEBI, Bank of Baroda Research Note:* Apr & May'22

Concluding remarks

The emerging picture on investment is one of cautious movement in certain sectors and is not yet broad based. New project announcements are only intentions and may not necessarily materialize in this year. Compared to previous years, the number is higher, though is much lower compared to Q4FY22. This is corroborated by growth in bank credit which is more retail oriented so far (data available for two months of the year). Debt issuances have been lower with 2/3 being issued by finance companies. ECB approvals also are lower. Quite clearly we may have to wait for the next few quarters to gauge the private investment mood. The higher interest rate scenario and inflation amidst continued global political uncertainty will be factors that will drive the pace of investment in the coming months.

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