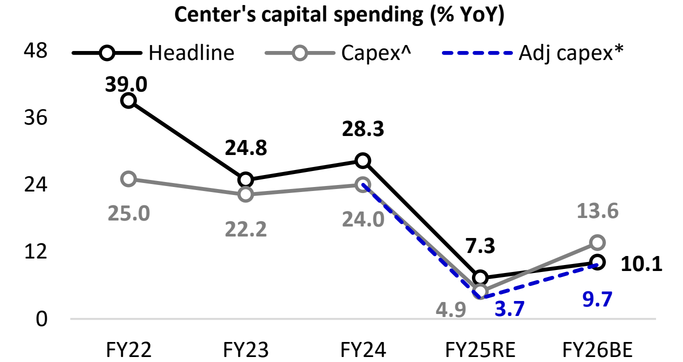
Low base to push combined capex growth to 13.4% in FY26BE

Budgeted at 3.7% of GDP in FY26, lower than in pre-Covid years

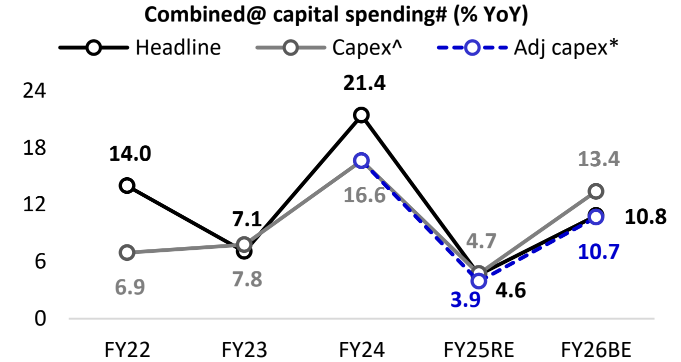
- **What is the budgeted capex growth and what should be included in the capex budget? The answers to these questions should not be a matter of confusion but they are. Therefore, we attempt these questions in this note.**
- **As of last year, the Center's budgeted capex estimates were widely quoted, which were growing at a fast pace. In the past many years, we have highlighted that off-budget capex (done by central public sector enterprises or CPSEs) must be included in the budgeted capex to find out the true capex estimates. While the inclusion of CPSEs is a widely accepted practice now, another line item – called 'grants for creation of capital assets' to states/UTs – is included in the budgeted and CPSEs capex this year to estimate growth in the Center's capex.**
- **Based on the headline data, growth in the Center's capital spending is revised to 7.3% YoY in FY25RE (from 16.9% YoY in FY25BE) and is budgeted to grow 10.1% YoY in FY26BE. CPSEs' capex is budgeted to grow 12.9% YoY in FY26BE, from a decline of 1.9% YoY in FY25RE (13.0% YoY in FY25BE), and the 'grants for creation of capital assets' are budgeted to grow at a 14-year high pace of 42.4% YoY in FY26BE, compared with a fall of 1.3% YoY in FY25RE (21.7% YoY in FY25BE). All combined, the aggregate capex is budgeted at INR19.8t in FY26BE from INR17.0t in FY25RE (INR18.7tn in FY25BE), implying a growth of 16.4% YoY next year, from a revised growth of 3.5% this year (from 17.1% YoY in FY25BE).**
- **There are good reasons why 'grants for creation of capital assets' should not be included in the Center's capex. Many of these schemes, such as MGNREGA or PM Surya Ghar Muft Bijli Yojana, are not capex, and more importantly, such expenditure on capital assets will be included in states' capex.**
- **Three further adjustments are needed to understand the true extent of the GoI's true capex: 1) The Center's capital spending has two parts – capital outlays/expenditure (or capex) and loans and advances (L&As). The latter must be excluded, as they would be included in states' capex; 2) The GoI has included the equity infusion of INR339b into BSNL in FY26BE under capex, which must also be excluded, as it does not have any capex multiplier; and 3) Investments of Food Corporation of India (FCI), within CPSEs capex, must be excluded since they are operational expenses.**
- **After adjusting these factors, the combined capex is budgeted to grow 13.4% YoY in FY26BE vs. 4.7% growth in FY25RE (revised from 14.3% YoY in FY25BE). Further, the GoI has included INR417b as 'New Schemes' under the Ministry of Finance, for which we could not find any details (vs. INR91b in FY25RE, revised from INR626b in FY25BE). The combined capex growth will ease to 10.7% YoY in FY26BE, from 3.9% YoY in FY25RE (8.5% YoY in FY25BE), if we exclude the allocation to 'New Schemes'.**
- **Overall, the combined capex is budgeted at 3.7% of GDP in FY26BE, better than 3.6% in FY25RE but lower than 3.8% of GDP in FY24 and 3.9% of GDP in the pre-Covid years.**

Exhibit 1: Center's capex budgeted to grow 10-14% YoY in FY26…



^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 11-13%



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

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What is the Center's true capex budgeted for FY26BE? Based on the headline data, the growth in the Center's capital spending is revised to 7.3% YoY in FY25RE (from 16.9% YoY in FY25BE) and is budgeted to grow 10.1% YoY in FY26BE. CPSEs' capex is budgeted to grow 12.9% YoY in FY26BE compared with a decline of 1.9% YoY in FY25RE (13.0% YoY in FY25BE).

We must, however, make three adjustments to the headline data to understand the extent of GoI's true capex. Let's discuss them one by one.

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

INR b, unless otherwise mentioned	FY23	FY24	FY25BE	FY25RE	FY26BE
Central government capital spending (Budgeted allocation)					
Ministry of Defense	**1,429**	**1,543**	**1,720**	**1,595**	**1,800**
Ministry of Railways	**1,593**	**2,426**	**2,520**	**2,520**	**2,520**
Ministry of Road Transport & Highways	**2,105**	**2,699**	**2,722**	**2,589**	**2,591**
Department of Telecommunications	**556**[1]	**605**	**844**	**750**	**502**
Capital infusion to BSNL	**266**	**568**	**831**	**721**	**339**
Police	**82**	**98**	**101**	**158**	**118**
Others[2]	**482**	**511**	**1,472**	**922**	**1,381**
Loans and advances (L&As)	**1,153**	**1,611**	**1,715**	**1,707**	**2,258**[3]
States/UTs/foreign governments	927	1,229	1,424	1,394	1,706
Total capital spending (% YoY)	**7,400 (24.8)**	**9,492 (28.3)**	**11,111 (16.9[4])**	**10,184 (7.3)**	**11,211 (10.1)**
Capital outlays (Capex, % YoY)[5]	6,207 (22.2)	7,695 (24.0)	8,856 (15.0[4])	8,070 (4.9)	9,166 (13.6)
Central Public Sector Enterprises (CPSEs)					
Ministry of Defense	28	32	33	36	41
Ministry of Railways	447	196	130	130	130
Ministry of Power	574	544	667	707	858
Ministry of Petroleum & Natural Gas	1,190	1,369	1,185	1,289	1,324
Ministry of Housing & Urban development	165	234	425	421	622
Food corporation of India (FCI)	305	477	270	250	280
Others	922	1,048	977	992	1,061
Total capital outlays (% YoY)	**3,631 (-17.0)**	**3,900 (7.4)**	**3,686 (13.0[4])**	**3,824 (-1.9)**	**4,316 (12.9)**
Total capex (Excluding FCI, % YoY)	**3,326 (-11.7)**	**3,423 (2.9)**	**3,417 (12.5[4])**	**3,574 (4.4)**	**4,036 (12.9)**
Combined capital outlays (Capex)[6]					
Ministry of Defense	1,457	1,575	1,753	1,631	1,841
Ministry of Railways	2,040	2,621	2,650	2,650	2,650
Ministry of Road Transport & Highways	2,105	2,699	2,722	2,589	2,591
Combined capex[6] (as a percentage of GDP)	**9,534 (3.5)**	**11,118 (3.8)**	**12,273 (3.7)**	**11,644 (3.6)**	**13,202 (3.7)**
YoY (%)	**7.8**	**16.6**	**14.3**[4]	**4.7**	**13.4**

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

[2]Includes INR626b/INR91b/INR417b in FY25BE/FY25RE/FY26BE as 'New Schemes' under MoF

[3]Includes INR200b for 'other scientific research'

[4]FY25BE over FY24RE

[5]Excluding capital infusion into PSUs and L&As to states

[6]Excluding capital infusion into PSUs, L&As to states and FCI's capex (but including 'New Schemes')

Source: Union Budget documents, MOFSL

Excluding L&As to states, the GoI's capex is budgeted at INR9.5t in FY26BE, up 8.1% YoY, following an average growth of 22% during FY21-FY25RE

a. **Segregate capital outlays (capex) from L&As:** 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 FY25 and they are budgeted to grow significantly to 20% in FY26, which is the highest share since FY05, barring FY21.

The GoI has budgeted L&As worth INR2.3t in FY26BE (32.3% YoY growth in FY26BE), including a transfer of INR1.7t to states. 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 FY26BE, up 8.1% YoY, following an average growth of 22% during FY21-FY25RE.

A total of INR1.89t has been allocated during the past four years as capital infusion into BSNL under the GoI's capital spending

b. **Equity infusion into PSUs must also be excluded:** A detailed ministry-wise analysis of the capex also reveals that the Department of Telecommunications (DoT) has included financial relief/capital infusion totaling INR266b into BSNL in FY23 (down from INR447b/INR333b in FY23BE/FY23RE), INR568b in FY24 (down from INR648b in FY24RE), INR721b in FY25RE (down from INR831b in FY25BE) and another INR339b in FY26BE. Thus, a total of INR1.89t has been allocated during the past four years as capital infusion into BSNL under the GoI's capital spending. These capital infusions pushed the allocation under the Ministry of Communications from less than INR40b in FY22 to INR750b in FY25RE and INR502b in FY26BE.

After excluding L&As to states and such financial support to various PSUs, the GoI's capex is budgeted to rise 13.6% YoY in FY26BE

After excluding L&As to states and such financial support to various PSUs, the GoI's capex is budgeted at INR9.2t, up 13.6% YoY in FY26BE, following an average growth of 20% during FY21-FY25RE *(Exhibit 3 on the preceding page)*. The growth in capital spending, excluding L&As to states and equity infusion into PSUs, is higher than the growth in headline capital spending because of a lower number budgeted for equity infusion into BSNL (INR339b in FY26BE vs. INR721b in FY25RE).

c. **'New Schemes' under the Ministry of Finance:** Further, the GoI has allocated a sum of INR417b as 'New Schemes' under other expenditure in the Department of Economic Affairs, Ministry of Finance (included under Others in *Exhibit 3* above). We could not find any details regarding this line item, just like in the FY25 budget. We understand that this amount could be allocated against some schemes that are work-in-progress but not sure about it. A similar allocation of INR626b was made in FY25BE, which is now revised down to INR91b in FY25RE. In fact, a large part of the downward revision in the Center's capex in FY25 was on account of this item, which makes us believe that the adverse economic impact was limited.

If we further exclude INR417b under 'New schemes', the GoI's adjusted capex is budgeted to grow 9.7% YoY this year

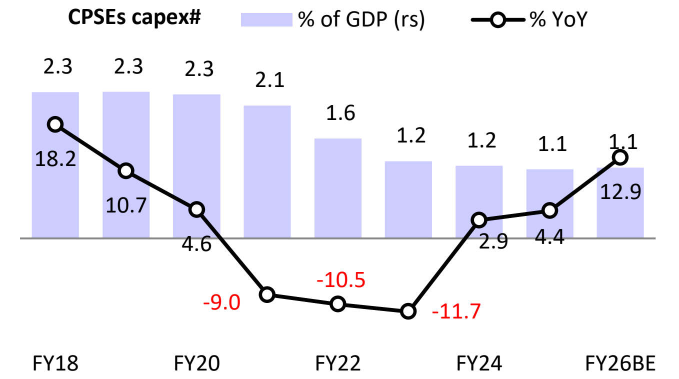
If we do not exclude 'New Schemes', the GoI's capex is budgeted to grow 13.6% YoY in FY26BE. However, if we further exclude INR417b, the GoI's adjusted capex is budgeted to grow 9.7% YoY this year *(see Exhibit 1)*.

Internal and Extra Budgetary Resources (IEBR) of CPSEs budgeted to grow at an eight-year high pace in FY26: 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 is the combined capital outlay of the GoI and CPSEs.

Excluding FCI, IEBR of CPSEs is budgeted to increase 12.9% YoY in FY26BE, the highest in eight years

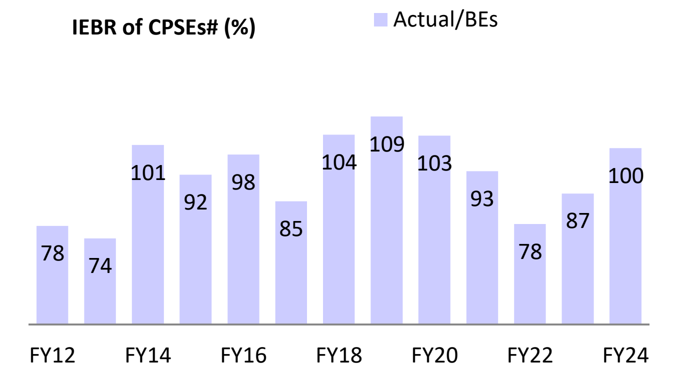
After making the above-mentioned adjustments in the GoI's investment spending, we have made one adjustment in CPSEs' capex. Since FY18, the DF&PD (which includes the allocation to FCI) has undertaken the maximum capital outlays among CPSEs, averaging about INR2t each year during FY18-FY20. As the GoI 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 four years (FY23-FY26BE). This, we believe, must be excluded from the aggregate IEBR of CPSEs to understand the true extent of the infrastructure push by the GoI. Excluding FCI, IEBR of CPSEs is budgeted to increase 12.9% YoY in FY26BE, the highest growth in the last eight years *(Exhibit 4)*.

Exhibit 4: CPSEs' capex (excl. FCI) is budgeted to increase at eight-year high pace of 12.9% YoY in FY26BE



#Excluding FCI allocations

Exhibit 5: Actual CPSEs' capex met BEs in FY24, though averaged 95% in the past decade



Source: Budget documents, CSO, MOFSL

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

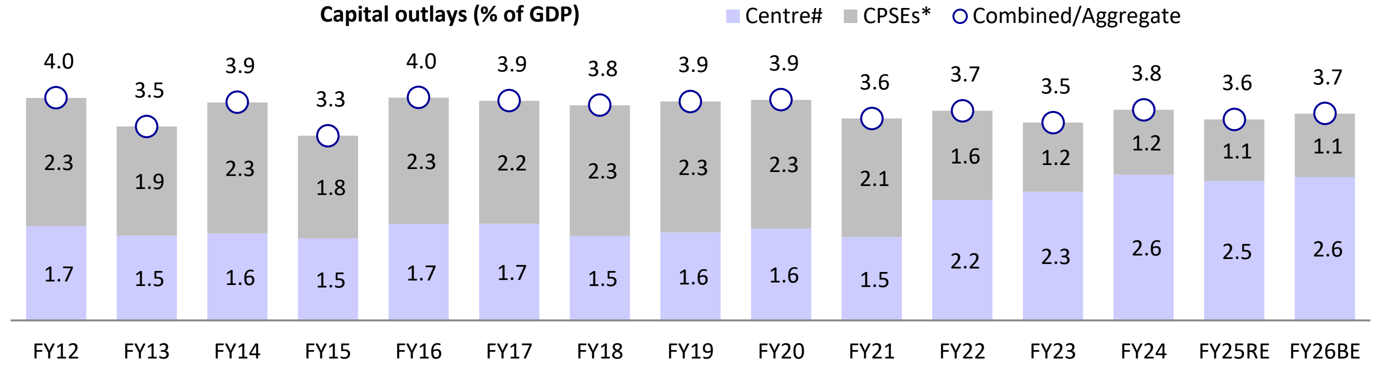
At the same time, historical data suggests actual capex by CPSEs tends to be about 90-95% of the budgeted and revised estimates (BEs/REs), with much sharper cuts vs. BEs in FY22 and FY23 *(Exhibit 5)*. CPSEs' capex was revised down to INR3t in FY24, from INR3.4t in FY24BE. However, in FY25RE, CPSEs capex was higher than what was budgeted (INR3.6t in FY25RE vs. INR3.4t in FY25BE). Therefore, it is not necessary that CPSEs' capex for FY26 would be revised lower.

The combined capex (of the Center and CPSEs) is budgeted at 3.7% of GDP in FY26, higher than 3.6% in FY25RE, but lower than the pre-Covid period

Low base pushes combined capex growth to 13.4% YoY in FY26BE; budgeted at 3.7% of GDP, lower than in pre-Covid years: 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 4.7% YoY in FY25RE and were budgeted to rise by 13.4% YoY in FY26 *(see Exhibit 2 above)*.

The combined capex, thus, is budgeted at 3.7% of GDP in FY26BE, better than 3.6% in FY25RE but lower than 3.8% of GDP in FY24 and 3.9% of GDP in the pre-Covid years *(Exhibit 6)*.

Exhibit 6: Combined capital outlays of the government and CPSEs



#Excluding L&As to states and equity infusion to PSUs *Excluding FCI

Source: Union Budget documents, CSO, MOFSL

After adjusting the Center's capex by INR417b allocated as 'New Schemes', the combined capex will fall to 3.6% of GDP this year

After adjusting the Center's capex by INR417b allocated as 'New Schemes' under the Ministry of Finance, the Center's capex growth will be 9.7% and the combined capex growth will be 10.7% YoY in FY26BE *(see Exhibit 2 above)*. Accordingly, the combined capex will fall to 3.6% of GDP next year.

'Grants-in-aid for creation of capital assets' must not be included in the Center's capex: Unlike in the past years, there is an argument that the grants-in-aid to states for the creation of capital assets should also be included in the Center's capex. Such grants are budgeted at INR4.3t in FY26BE, with a 14-year high growth of 42.4% YoY, compared with a fall of 1.3% YoY in FY25RE (21.7% YoY in FY25BE). If we add these grants to the combined capex discussed above, the aggregate capex is budgeted at INR19.8t in FY26BE from INR17.0t in FY25RE (INR 18.7tn in FY25BE), implying a growth of 16.4% YoY next year, compared with revised growth of 3.5% this year (from 17.1% YoY in FY25BE).

There are good reasons why 'grants for creation of capital assets' should not be included in the Center's capex. Many of these schemes, such as MGNREGA or PM Surya Ghar Muft Bijli Yojana, are not capex *(Exhibit 7)*.

Exhibit 7: Key allocations under 'Grants for creation of capital assets'

(INR b)	FY23	FY24	FY25BE	FY25RE	FY26BE
MGNREGA	902	888	853	853	854
Jal Jeevan mission/National Rural drinking water mission	507	647	651	210	625
Pradhan Mantri Awaas Yojana – Gramin (PMAY-G)	411	192	506	286	509
PM Surya Ghar Muft Bijli Yojana – New & renewable energy	…	…	56	102	190
Pradhan Mantri Gram Sadak Yojna (PMGSY)	189	140	189	144	189
Pradhan Mantri Awaas Yojana – Urban (PMAY-U)	154	197	236	115	172
Reform Linked Distribution Scheme – Power	25	98	123	124	158
Transfer to states	70	65	193	190	150
Urban challenge fund	…	…	…	…	100
Road works	75	86	87	87	95
Others	730	726	1,031	888	1,229
Total (% YoY)	**3,063 (26.2)**	**3,039 (-0.8)**	**3,908 (21.7)**	**2,999 (-1.3)**	**4,272 (42.4)**

Arranged as per top 10 schemes in FY26BE Source: Union Budget documents, CSO, MOFSL

Just like the Center's loans, if these grants are spent on capex by states, then they would form a part of states' capex. Therefore, we must exclude them from the Center's budgeted capex to avoid double counting.

Just like the Center's loans, if these grants are spent on capex by states, then they would form a part of states' capex

Interestingly, it is not clear if the states classify all these expenditures as capex. For instance, the Center's grants to states for capital assets' creation under the Department of Rural Development (excluding MGNREGA and considering only PMAY-G and PMGSY) totaled INR420b/INR600n in FY22/FY23. In contrast, states' aggregate capex under this Department was lower at about INR300b and INR400b, respectively.

If one argues that a lot of spending under such grants actually represents capex, and thus, should ideally be included under capex, then one must also note that a part of spending under capex budget is actually current expenditure (wages/salaries etc.), and thus, should be excluded. Since such reclassification is impossible for any outsider (and not sure if even the government can conduct such an exercise), it is better to estimate capex budget under the existing classifications.

Therefore, we keep grants for the creation of capital assets outside the capex estimates.

Accordingly, the combined capex of the Center and CPSEs (excluding loans & advances to states, capital infusion into PSUs and FCI's capex) is budgeted to grow 13.4% of GDP in FY26, supported by a low base of 4.7% in FY25RE (revised down from 14.3% in FY25BE). It is budgeted at 3.7% of GDP in FY26, slightly better than 3.6% of GDP in FY25RE, but lower than in the pre-Covid years (or 3.8% in FY24).

Overall, for the first time in almost a decade, the GoI focused more on consumption and savings rather than capex. We need to keep a keen eye on whether this change is a one-off or if it suggests a change in the paradigm.

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