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Is India Inc. deleveraging?

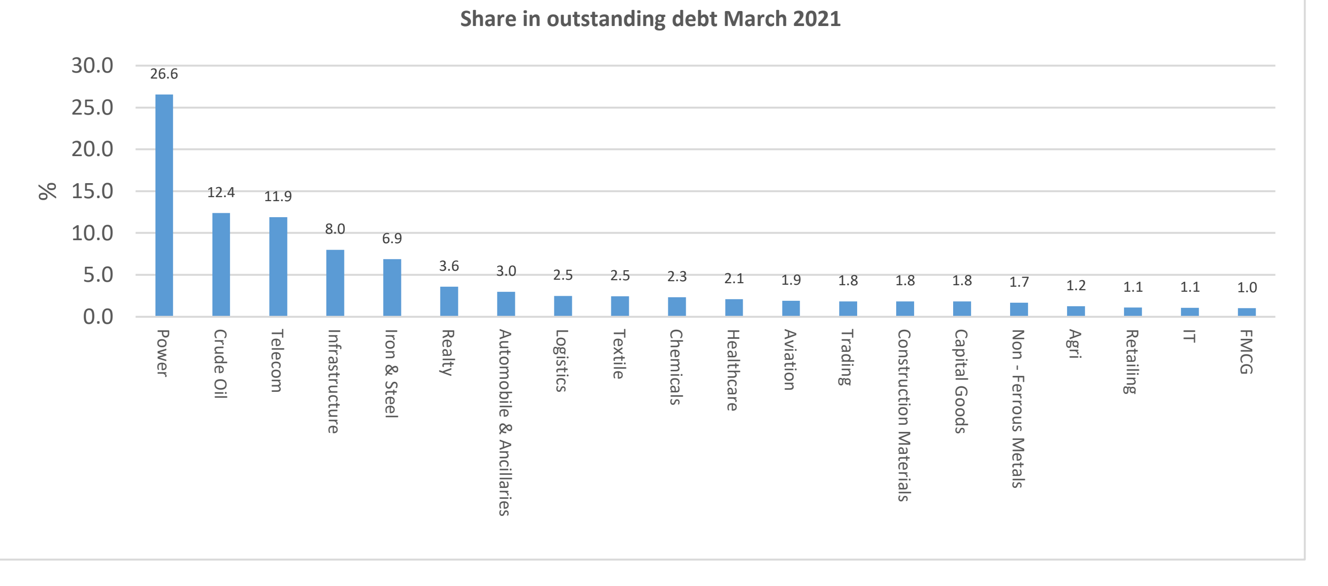
A trend which is picking up in corporate India is that companies are deleveraging as witnessed by the overall level of debt of various sectors coming down. This is notwithstanding the fact that there has been a very favorable interest rate regime since the lockdown was announced which should have made borrowing easier. However, there have been other forces at play which has led to a slowdown in growth of debt of companies. How far is this true?

For purpose of this analysis a sample of 4827 non-finance companies have been considered across 36 major sectors for the period of 2016-17 to 2020-21. The outstanding debt of these companies as of March 2021 was Rs 41.07 lakh crore which is around 20% of nominal GDP in FY21. Debt for these companies had increased by a CAGR of 4.5% during this period against a CAGR of 2.4% in real GDP. If FY21 is excluded given that it was a black swan year, then the CAGR in debt would be 6.9% per annum for the 3-years period while GDP growth would be 5.8%. In FY21, GDP growth rate fell by 6.6% and debt by 2.5%.

Hence there has been a tendency for debt of corporates to increase at a faster rate than the real GDP growth rate. But this is the aggregate picture and a disaggregated analysis is required to understand whether such growth has been witnessed across most sectors or not.

Where is debt concentrated?

The chart below gives the shares of various sectors in total debt of the sample companies as of March 2021. All sectors with a share of above 1% in total have been included.



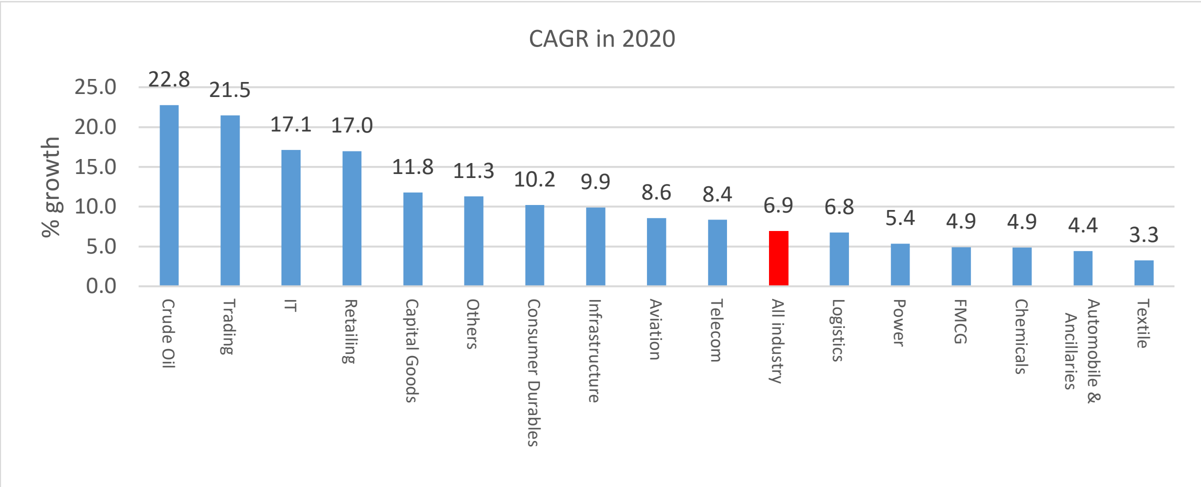
Source: BOB Economic Research

As can be seen from the chart, there is concentration in the sectors that require heavy investment and would require progressively more finance as India focuses on an investment led growth path in future in the tryst to attain the $ 5 trillion economy. The top five sectors: power, crude oil, telecom, infrastructure and iron and steel had a share of a little more than 2/3 of total debt at 65.8%. The next 6 sectors with shares individually of more than 2% each were realty, automobiles, logistics, textiles, chemicals, and health care. Their combined share was 15.9%. Combining the two, 81.7% of total debt was concentrated in 11 broad sectors.

Which sectors have witnessed higher growth in debt?

For addressing this question, FY21 needs to be excluded as in in this year, overall outstanding debt decreased by 2.5% due to the lockdown. On account of limited operations of business several sectors were affected in terms of both investment and production which in turn led to outstanding debt coming down. Incremental debt was down by Rs 1.04 lakh crore as against an increase of Rs 3.10 lakh crore and Rs 3.08 lakh crore in FY19 and FY20 respectively.

The chart below gives the CAGR in o/s debt for the leading sectors for the period FY17-FY20. Besides the sectors that require heavy investment, it can be seen that services have witnessed smart increase in debt levels like trading, IT, retailing, and logistics besides aviation.

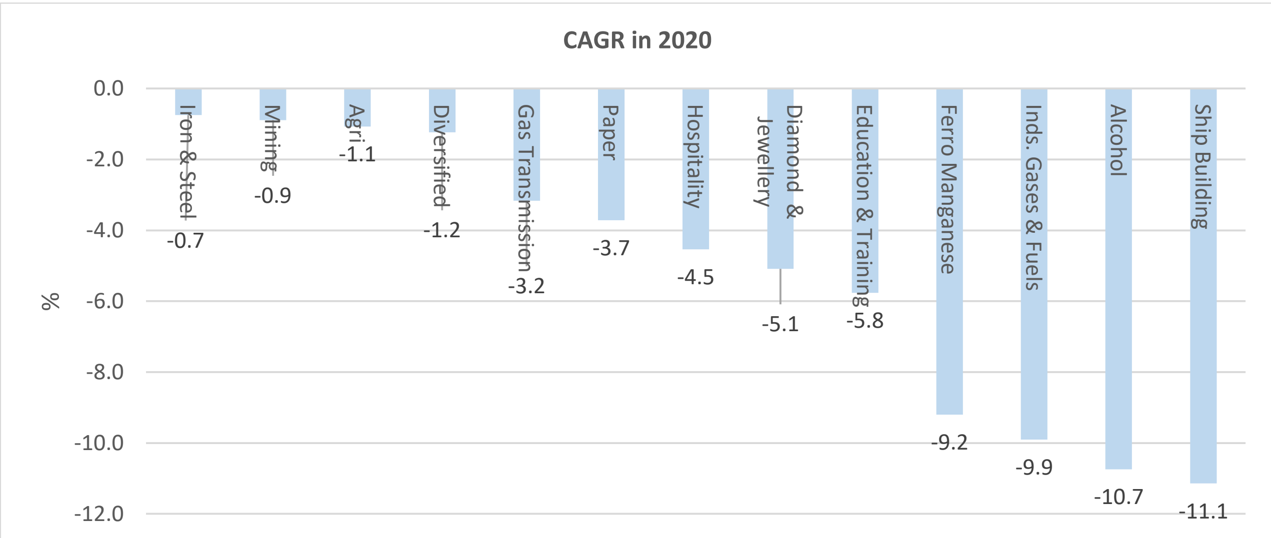


Source: BOB Economic Research

Sectors like trading, retailing, telecom, logistics etc. witnessed a boom as online mode was adopted for selling goods. Higher use of mobile phones led to a boom for the telecom sector too.

Where has deleveraging taken place?

The chart below provides an illustration of the industries where the growth in o/s debt has cumulatively been negative implying that there has been a reduction in the level of debt.



Source: BOB Economic Research

While prima facie it may appear that deleveraging would have accelerated during the pandemic, interestingly, the process had started earlier. There were 1842 and 1899 companies respectively in FY18 and FY19 which had witnessed a drop in their debt levels. Subsequently the number of companies deleveraging increased to 2139 in FY2020 and 2144 further in FY21.

In terms of number of sectors, 20 witnessed fall in debt in FY21 as against 14 in FY20 and FY19. This also means that deleveraging is something being witnessed for the last few years and is not purely a pandemic related phenomenon.

The reasons for debt levels coming down are:

- Insolvency resolution has contributed to an extent as assets sold have been used to compensate creditors.
- Companies have not been borrowing afresh due to the state of the industry. With most industries having surplus capacity then incentive to invest has been limited which had resulted in debt repayments being higher than fresh borrowing. The average capacity utilization rate as per RBI had come down to 47.3% in Q1 of FY21 and finally recovered to 69.4% in Q4-FY21.
- Some have used their cash surpluses for repaying expensive debt or used the same for expanding capacity. In steel for example, there has been high capacity utilization and investment is being largely financed from internal resources.
- Some companies have sold off assets and used the proceeds to repay debt.
- Those that are still going through the insolvency process have been borrowing minimum sums from the banking system.
- Companies have also lowered their debt levels to improve their credit profile and used restructuring as a tool to achieve this.
- The buoyant equity markets has also been an option for companies to raise funds at the margin.
- Overall investment in the economy had reached the lowest level as denoted by the gross fixed capital formation rate of 26.6% in FY21.

Will this trend continue? On one hand it has been seen that companies have been repaying debt or using their own funds for further investment. But the future investment scene is positive and there would be large doses of capital required especially in the area of infrastructure. The government too is going in for asset sale which will finally have to be funded by the financial system. Therefore there will be large requirement for funds. The corporate bond market which is hitherto one for higher rated entities will continue to grow. But the bulk of the financing will come from the banking system which will also have to reorient itself to this challenge given that in the last 5 years or so after the emergence of the NPA challenge, there has been a conscious shift to retail lending. It may hence be concluded that this trend of deleveraging will have to turn around as the investment cycle picks up and accelerates. This was expected to commence in FY23 but will get delayed due to the war.

Appendix:

Sector profile: Outstanding debt (Rs crore)

Sector	Number	2017	2018	2019	2020	2021
Power	154	9,12,353	9,52,460	10,30,795	10,67,263	10,91,023
Crude Oil	33	3,22,928	3,17,480	3,98,339	5,97,513	5,09,411
Telecom	44	3,18,192	3,67,580	4,64,637	4,04,813	4,88,438
Infrastructure	253	2,44,312	2,70,787	2,86,927	3,24,232	3,28,381
Iron & Steel	224	3,36,127	3,36,101	3,04,662	3,28,662	2,83,257
Realty	253	1,46,220	1,62,690	1,65,961	1,58,346	1,47,159
Automobile & Ancillaries	342	1,06,329	1,03,959	1,10,121	1,21,033	1,21,499
Logistics	112	81,921	82,124	91,605	99,733	1,02,380
Textile	388	1,04,900	1,12,743	1,12,267	1,15,468	1,00,847
Chemicals	274	1,08,378	1,03,548	1,18,657	1,25,050	95,559
Healthcare	281	89,433	1,00,655	1,03,432	94,416	85,921
Aviation	13	58,120	64,359	70,349	74,375	77,808
Trading	290	40,944	47,215	50,073	73,374	75,714
Construction Materials	139	82,567	77,030	80,655	83,542	75,610
Capital Goods	437	56,139	59,875	65,341	78,376	75,114
Non - Ferrous Metals	60	79,991	71,089	72,185	81,103	68,853
Agri	207	54,271	52,039	50,801	52,548	50,930
Retailing	52	20,669	22,094	31,350	33,091	45,005
IT	178	28,618	32,511	39,470	45,991	43,200
FMCG	230	37,352	42,305	44,486	43,131	42,213
Others	150	19,257	20,616	23,294	26,537	28,786
Media & Entertainment	124	26,967	30,489	32,689	29,343	23,318
Hospitality	88	24,281	24,322	23,611	21,128	22,705
Plastic Products	136	19,682	19,013	18,298	20,282	18,424
Paper	66	19,235	16,822	15,977	17,169	18,289
Mining	29	19,103	15,538	15,916	18,597	16,067
Diamond & Jewellery	44	16,729	19,714	19,086	14,305	15,600
Diversified	21	19,777	21,151	17,489	19,057	15,345
Inds. Gases & Fuels	21	15,003	11,326	9,079	10,972	12,010
Electricals	67	8,161	8,667	8,436	8,405	8,761
Consumer Durables	47	7,004	7,091	9,527	9,374	7,940
Alcohol	27	9,214	8,105	7,610	6,552	4,790
Gas Transmission	6	5,211	8,110	6,654	4,732	3,342
Education & Training	20	1,640	1,940	1,582	1,372	1,486
Ferro Manganese	10	1,617	1,573	1,423	1,211	1,240
Ship Building	7	1,168	1,212	1,299	820	742
All companies	**4,827**	**34,43,813**	**35,94,330**	**39,04,082**	**42,11,915**	**41,07,167**

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