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CAPITAL EXPENDITURE

SYLLABUS:

GS 3 > Basic Economics

REFERENCE NEWS:

The government's capital expenditure has surged sharply in the first five months of FY26. The Centre has already spent nearly 39% of its annual outlay of 11.2 trillion INR, marking a robust 43% year on year jump. The general government capex as a share of GDP in FY26 is likely to remain around 5% which is lower than past 2 financial years.

CAPEX IN INDIA:

Capital Expenditure (Capex) refers to long-term investments made by the government or private entities in acquiring, creating, or upgrading **physical assets** such as buildings, infrastructure, machinery, or technology.

- Unlike **Operating Expenditure (Opex)**, which covers day-to-day expenses, Capex contributes to **asset creation**, long-term productivity, and **sustained economic growth**.
- Capex is a **countercyclical fiscal tool**, stabilizes the economy during global uncertainties and stimulates private investment through the "crowding-in effect."
- It also has a **high multiplier effect**, generating significant employment and output.
- **State-Level Capex Trends:** States contribute about **40% of India's total Capex**, mainly in roads, irrigation, and urban infrastructure. However, several states underutilize their Capex budgets due to fiscal constraints and delayed fund release.

Government Capital Expenditure

- The **Union Budget 2025–26** earmarked **₹11.21 lakh crore** for Capex, which is **3.1% of GDP**, continuing the government's focus on infrastructure-led growth. This represents a **steadily rising trend** from ₹5.5 lakh crore in FY2021–22 to ₹9.5 lakh crore in FY2024–25, an **increase of over 100% in 4 years**
- Union Capex typically consists of:
 - **Capital Support:** Equity infusions into central ministries, public sector undertakings, and infrastructure projects.
 - **Loans and Advances:** Financial assistance to states and agencies to fund capital outlays.
- Notably, **loans and advances now form about 20% of total Capex in FY2025–26**, up from **18% in FY2024–25** and **9.9% in FY2021–22**, marking a structural shift in how the Centre finances development spending.

- The Capex push focuses on:
 - **Transport Infrastructure:** PM Gati Shakti, Bharatmala, Sagarmala.
 - **Railways:** ₹2.5 lakh crore allocation in FY25.
 - **Energy Transition:** Green hydrogen, renewable energy parks, and EV infrastructure.
 - **Defence Modernisation:** 68% of defence capital procurement reserved for domestic industry (2024).

Private Sector Capex (NSO Forward-Looking Survey, 2024)

- **Private sector Capex** grew **66.3%** between **FY2021–22 and FY2024–25**.
- However, it is **projected to decline by 25.5%** in **FY2025–26**, signalling cautious investment sentiment amid global headwinds, high borrowing costs, and weak external demand.
- **Sectoral distribution (FY2025):**
 - **Manufacturing:** 43.8%
 - **Information & Communication:** 15.6%
 - **Transport & Storage:** 14%
 - **Electricity, Gas & Energy supply:** Leading in Gross Fixed Assets (GFA) accumulation.
- **Nature of investments:**
 - 49.6% Income generation
 - 30.1% Upgradation
 - 2.8% Diversification
- **Growth in Gross Fixed Assets (GFA):** Average **GFA per enterprise** in the private corporate sector rose **27.5%**, from ₹3,279 crore (FY23) to ₹4,183 crore (FY24). Indicates expansion in productive capacity, particularly in manufacturing and power sectors.

Sectoral Distribution and Performance

Sector	Capex Trend (FY2025–26, Apr–Aug)	Observation
Railways	↑ 8% to ₹1.1 trillion	Sustained momentum under PM Gati Shakti & Vande Bharat expansion
Roads & Highways	↑ 11% to ₹1.17 trillion	Key focus on expressways, Bharatmala & logistics corridors
Telecommunications	↑ to ₹17,853 crore	Driven by 5G rollout and BharatNet digital infrastructure
Defence, Police, North-East, S&T, Space	↑	Reflects push for Atmanirbhar Bharat and strategic capabilities
Food & Public Distribution	↑ to ₹50,000 crore (from ₹335 crore)	Driven by loans to FCI to reduce bank borrowings

Sector	Capex Trend (FY2025–26, Apr–Aug)	Observation
Housing & Urban Affairs	↓ by 4% to ₹9,781 crore	Reflects moderation after Smart Cities and PMAY phases
Atomic Energy	↓ by 6%	Lower capital intensity in new projects

SIGNIFICANCE OF CAPITAL EXPENDITURE IN INDIA:

- **High Multiplier Effect on Economic Growth:** Capex generates a **multiplier effect** every ₹1 spent can yield ₹2.45–₹3.10 in economic output (as per RBI and NIPFP estimates).
 - **National Infrastructure Pipeline (NIP)** projects ₹111 lakh crore investment by 2025, expected to add 200 basis points to GDP growth.
- **Job Creation and Skill Development:** Infrastructure projects in roads, housing, and railways have high **employment elasticity**.
 - **PM Gati Shakti** and **National Logistics Policy** have boosted employment in construction and logistics sectors, while **Make in India** enhances industrial jobs.
- **Productivity Enhancement and Competitiveness:** Private Capex in sectors like manufacturing and IT improves efficiency and global competitiveness. India's **manufacturing GFA (Gross Fixed Assets)** grew 27.5% YoY in 2023–24, led by electronics, automobile, and steel sectors.
- **Countercyclical Fiscal Tool:** During economic slowdowns or weak private investment, **public Capex acts as a stabilizer**. The Union Government's 43% Capex rise in Apr–Aug 2025 offsets subdued private investments, ensuring sustained growth momentum.
- **Crowding-In Effect on Private Investment:** Sustained public Capex in infrastructure **reduces logistics and energy costs**, thereby encouraging private sector participation.
 - **PLI Scheme (₹1.97 lakh crore)** for 14 sectors has leveraged over ₹7 lakh crore in private Capex commitments.
- **Long-Term Asset Creation:** Public Capex results in durable assets, highways, power plants, airports, ports, and digital infrastructure, strengthening national productivity.
 - The **Bharatmala** and **Dedicated Freight Corridor** projects have enhanced logistics efficiency, while **Digital India** initiatives expand digital public infrastructure.
- **Catalyst for Inclusive and Regional Development:** Public Capex in backward regions (e.g., North-East, Aspirational Districts Programme) fosters **balanced regional growth**. The **North-East Development Capex** saw a significant rise in FY2025–26, improving connectivity and local economic activity.
- **Supports Private Capex Revival:** Public Capex helps reduce private investment uncertainty by improving infrastructure, credit flow, and market accessibility. Sectors such as **renewable energy, semiconductors, and EV manufacturing** are seeing public-private Capex synergy.

CHALLENGES OF CAPITAL EXPENDITURE IN INDIA:

- **High Borrowing Costs and Limited Access to Finance:** Elevated interest rates and tighter liquidity conditions have made large-scale project financing costlier. **Private firms** are increasingly relying on **internal accruals rather than external borrowing**, reducing new greenfield projects.

- NSO's Forward-Looking Survey (2025) shows that private Capex is projected to decline by 25.5% in FY2025–26 due to high financing costs.
- MSMEs face additional challenges due to limited access to formal credit, despite schemes like ECLGS and CGSS.
- **Low Capacity Utilisation in Industries:** Many industries are not fully utilising existing capacities, discouraging new investments.
 - The RBI Industrial Outlook Survey (Q3 FY2024) reports average capacity utilisation at 74.7%, down from 76.3% in Q4 FY2023.
 - Without stronger demand, companies hesitate to invest in expanding productive capacity particularly in sectors like **cement, steel, and automobiles**.
- **Delays in Land Acquisition and Project Clearances:** Lengthy approval processes and litigation under the **Right to Fair Compensation and Transparency in Land Acquisition Act, 2013** delay project execution.
 - The **Project Monitoring Group (PMG)** under the Cabinet Secretariat has identified over **300 large infrastructure projects** stalled due to land and environment clearance issues.
 - These delays lead to cost overruns, the **CAG (2023)** found that 37% of central infrastructure projects were delayed by over 2 years.
- **Geopolitical and Global Trade Uncertainties:** The rise in global protectionism and trade disruptions (e.g., **US–China tariffs, Ukraine–Russia conflict, Red Sea crisis**) has increased raw material and logistics costs. Export-dependent manufacturing firms in sectors like **electronics, chemicals, and textiles** are holding back Capex plans due to uncertain demand and input price volatility.
- **Structural Bottlenecks in Labour and Skills:** India faces a **paradox of labour abundance but skill scarcity**.
 - Large companies like **Larsen & Toubro (L&T)** reported difficulties in hiring **40,000 skilled workers** for ongoing projects.
 - Absence of flexible labour laws and persistent informalisation (over **85% of the workforce**) reduce the productivity benefits of new Capex.
- **Inefficiency and Quality Concerns in Public Capex:** While public Capex has risen sharply **43% increase to ₹4.31 trillion (Apr–Aug 2025)**, much of it is concentrated in loans and advances (20% of total), not direct asset creation.
 - The **Food and Public Distribution Department**, for instance, received ₹50,000 crore (from ₹335 crore last year), raising questions about the composition and growth impact of Capex.
 - Sectors like **Housing & Urban Affairs** saw a **4% decline**, and **Atomic Energy** fell by **6%**, indicating uneven prioritisation.
- **Overdependence on a Few Large Corporates:** Private Capex is heavily concentrated among large business groups such as **Reliance, Adani, and Tata**, while mid-sized firms lag behind. This skew limits broader participation and job creation.
 - According to the **Centre for Monitoring Indian Economy (CMIE)**, the top 10 corporate groups account for **over 60% of all new private Capex projects** in FY2024–25.
- **Weak Consumer Demand and Wage Stagnation:** Weak demand in rural and low-income segments constrains business confidence. **Real wage growth** is projected to decline from **7% in FY2025 to 6.5% in FY2026**, despite corporate profits being at a **15-year high (FY2023–24)**.
- **Limited Greenfield Investment and Innovation:** Most current private Capex is **brownfield** (expansion/upgradation), not new capacity creation.

- **R&D investment** remains low at **0.64% of GDP**, with only **36% contributed by the private sector**, compared to 70% in China and the U.S. This limits innovation-led capital formation and future competitiveness.
- **Implementation and Coordination Challenges in Public Projects:** Fragmented execution between the **Centre, States, and PSUs** often leads to inefficiencies.
 - Despite initiatives like **PM Gati Shakti** and **National Infrastructure Pipeline (NIP)**, lack of real-time coordination delays asset monetisation and project delivery.

Examples of Capex Inefficiencies

- **Railways and Roads:** While allocations have increased (Railways ₹1.1 trillion, Roads ₹1.17 trillion), project completion rates remain uneven.
- **Urban Infrastructure:** Capex under Smart Cities Mission faces significant delays, only **65% of projects completed** as of 2024 (MoHUA report).

WAY FORWARD:

Strengthen Institutional Coordination and Project Monitoring

- **Kelkar Committee on PPPs (2015):** Urged creation of an independent **PPP Appraisal and Monitoring Authority** to improve transparency, avoid contractual disputes, and ensure timely completion.
- The **United Kingdom's Major Projects Authority** conducts quarterly performance audits of public projects — a model India can emulate for accountability.

Ensure Quality and Productivity of Capex, Not Just Quantity

- **15th Finance Commission (2020)** recommended performance-linked grants for states to incentivise efficient use of capital funds.
- Introduce **Outcome-Based Budgeting** and regular **Public Asset Utilisation Reviews** to assess productivity and economic returns.
- **Tamil Nadu Infrastructure Development Board** evaluates projects based on their Gross Value Added (GVA) impact, a replicable model for other states.

Diversify Sources of Financing and De-Risk Investments

- **Rangarajan Committee on Financial Sector Reforms (2008)** suggested deepening corporate bond and infrastructure debt markets
- Promote **Infrastructure Investment Trusts (InvITs)** and **Real Estate Investment Trusts (REITs)** to crowd-in private investment while sharing risks.
- The **National Highways Authority of India (NHAI)** successfully raised over ₹25,000 crore through InvITs, an example of sustainable asset monetisation.

Empower States through Targeted Capital Incentives

- Adopt a **“Reform-Linked Capex Grant”** model like the **Scheme for Special Assistance to States for Capital Investment**, which rewards states that implement power, labour, and logistics reforms.
- The Union Government can expand this scheme beyond FY2026 to strengthen cooperative federalism and balanced regional infrastructure development.

Enhance Private Sector Participation and Greenfield Investment

- **N.K. Singh Committee on FRBM (2017)** suggested maintaining capital expenditure during fiscal consolidation to crowd-in private investment.
- Expand the **National Infrastructure Pipeline (NIP)** and integrate it with **sector-specific Production Linked Incentive (PLI)** schemes to attract private and foreign investors.

Improve Credit Availability and De-Risk Project Financing

- Expand **Credit Guarantee Schemes** for MSMEs and mid-sized manufacturers beyond startups.
- Strengthen the role of the **National Bank for Financing Infrastructure and Development (NaBFID)** to fund viable infrastructure projects with long-term, low-cost capital.

Strengthen Human Capital and Institutional Capacity

- Establish **Infrastructure Skill Development Councils** to train engineers, project managers, and financial analysts.
- Encourage technology-driven project management using **Building Information Modelling (BIM)**, **AI-based monitoring**, and **remote sensing** for real-time updates.

Promote R&D and Innovation-Linked Capex

- Offer **weighted tax deductions for R&D Capex** and create **sectoral research funds** (as recommended by the **Science, Technology, and Innovation Policy, 2021 Draft**).
- The **U.S. R&D Tax Credit Program** has driven significant private innovation and Capex in technology and manufacturing.

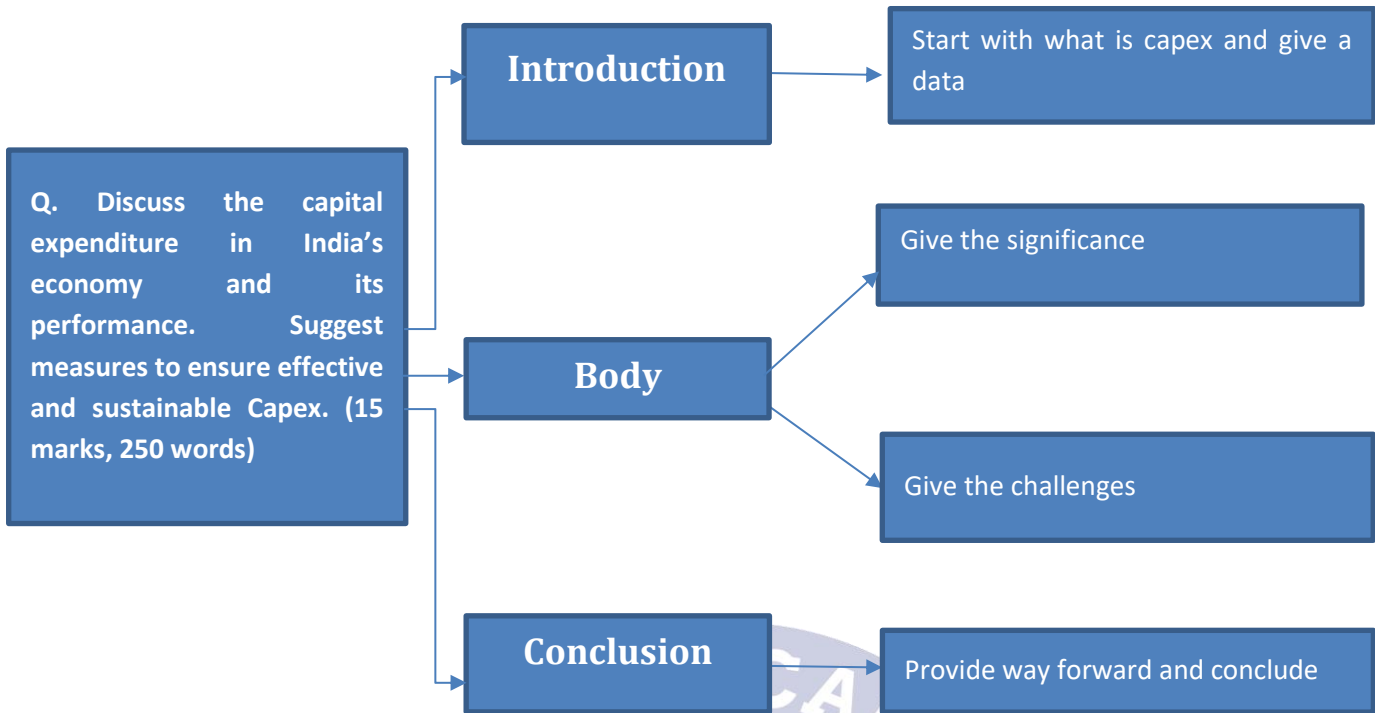
Focus on Sustainable and Green Infrastructure

- Prioritise green Capex in renewable energy, waste management, and urban mobility.
- Adopt **Green Budgeting Frameworks**, aligning with India's **LiFE (Lifestyle for Environment)** mission and **National Infrastructure Pipeline (NIP)** sustainability goals.

PRACTICE QUESTION:

Q. Discuss the capital expenditure in India's economy and its performance. Suggest measures to ensure effective and sustainable Capex. (15 marks, 250 words)

APPROACH:



MODEL ANSWER:

Capital Expenditure refers to long-term investments made by the government or private entities in acquiring, creating, or upgrading physical assets such as infrastructure, machinery, or technology. In India, Capex has gained renewed policy importance, with the **Union Government allocating ₹11.21 lakh crore (3.1% of GDP) for FY2025–26, marking over a 100% increase since FY2021–22.**

Significance of Capital Expenditure

1. **High Multiplier Effect on Growth:** Every ₹1 spent on Capex generates ₹2.45–₹3.10 in economic output (RBI, NIPFP estimates).
2. **Employment Generation and Skill Creation:** Infrastructure projects in roads, housing, and railways have high employment elasticity. **PM Gati Shakti** and the **National Logistics Policy** have created thousands of jobs in logistics and construction.
3. **Productivity and Competitiveness Boost:** Private Capex, particularly in manufacturing, electronics, and steel, enhances industrial productivity. Manufacturing sector **GFA grew 27.5% YoY in 2023–24**, reflecting rising efficiency.
4. **Countercyclical Fiscal Tool:** During global slowdowns, public Capex sustains momentum. The Centre's Capex rose **43% in April–August 2025**, offsetting weak private investment.
5. **Crowding-In Private Investment:** Public Capex lowers logistics and energy costs, encouraging private sector Capex. The **PLI Scheme (₹1.97 lakh crore)** has attracted over **₹7 lakh crore in private investment.**

6. **Regional and Inclusive Growth:** Capex in the **North-East and Aspirational Districts** boosts balanced development. Investments in **urban infrastructure and rural connectivity** improve access to jobs and markets.

Challenges in India's Capex Performance

1. **High Borrowing Costs and Financing Constraints:** Private firms face high interest rates; **private Capex projected to fall by 25.5% in FY26** (NSO). MSMEs still struggle to access formal credit despite schemes like ECLGS and CGSS.
2. **Low Industrial Capacity Utilisation:** Average utilisation at **74.7% (RBI Q3 FY24)** discourages new investments.
3. **Delays in Land and Environmental Clearances:** **CAG (2023)** found 37% of central projects delayed over two years due to land issues. Over **300 major projects** remain stalled (PMG data).
4. **Quality Concerns in Public Capex:** Loans and advances form **20% of total Capex**, often not translating into asset creation.
5. **Overdependence on Large Corporates:** Top 10 corporate groups (Reliance, Tata, Adani) account for **over 60% of new private Capex (CMIE)**, limiting inclusive growth.
6. **Global Uncertainties and Supply Chain Risks:** Conflicts like **Ukraine–Russia and Red Sea crises** raise input costs, making firms cautious in long-term Capex.

Way Forward

1. **Outcome-Based and Quality-Oriented Capex:** As per **15th Finance Commission (2020)**, link grants to performance and asset quality. Tamil Nadu's **Infrastructure Development Board** evaluates projects via **Gross Value Added (GVA)** impact — a replicable best practice.
2. **De-Risk Financing and Deepen Capital Markets:** Promote **InvITs and REITs** as per **Rangarajan Committee (2008)** to attract private funds. **NHAI** raised ₹25,000 crore via InvITs — a model for other infrastructure PSUs.
3. **Empower States through Reform-Linked Incentives:** Expand **Special Assistance to States for Capital Investment** beyond FY26 to promote cooperative federalism.
4. **Private Sector and Greenfield Boost:** **N.K. Singh Committee (2017)** advised maintaining Capex during fiscal consolidation to crowd-in private investment. Integrate Capex with **PLI and NIP** for renewable energy, EVs, and semiconductors.
5. **Human Capital and Innovation Push:** Establish **Infrastructure Skill Development Councils** and promote R&D-linked Capex (India's R&D spend only 0.64% of GDP). Provide **weighted tax deductions for R&D** as per the **STI Policy, 2021 draft**.
6. **Sustainable and Green Capex Focus:** Implement **Green Budgeting Frameworks** aligned with India's **LiFE Mission** for environment-friendly investments.

Capital expenditure remains the **engine of India's economic transformation**, with the government leading an infrastructure-driven growth strategy. However, for Capex to yield its full multiplier impact, India must ensure **quality over quantity, broader private participation, and institutional efficiency**.

