

INDIA'S SAVINGS & INVESTMENT ON A HIGHER TREND WITH A CONCOMITANT DECLINE IN ICOR: INTERPRETATIONS OF GDP GROWTH BASED ON NOISY QUARTERLY NUMBERS IS A GAME OF SMOKE AND MIRROR

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India's quarterly Y-o-Y GDP growth has been in a declining trend in FY23 sequentially, prompting arguments that India's growth is reminiscent of a pre 1980 Raj Krishna coined growth rate. Apart from the fact that, quarterly growth numbers are noisy and should be best avoided for any serious interpretation (on an average, India's GDP growth has witnessed Rs 2 lakh crores upward revision for the 3 year ended FY23), we find such argument ill-conceived, biased and pre-mature at its best when weighing the recent GDP numbers against the available data on savings and investments.

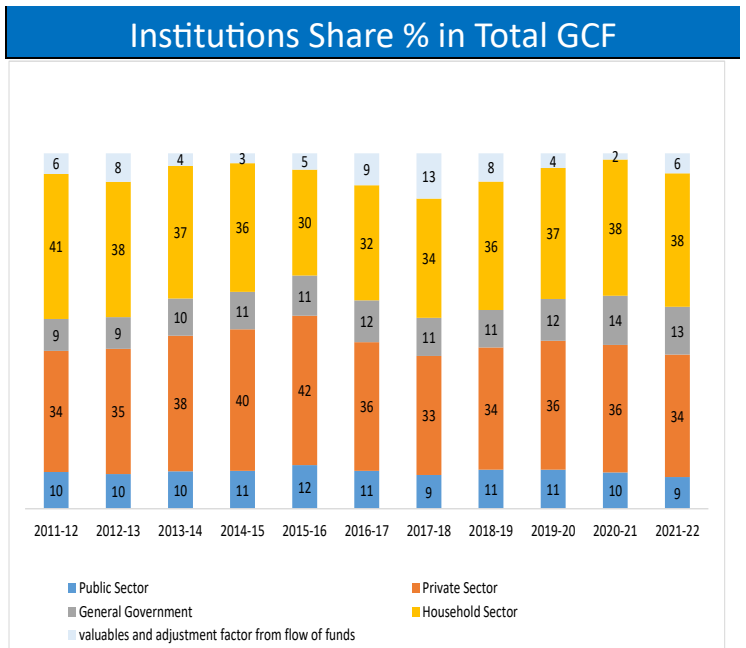
The investment and savings data for the past decade reveals interesting points (All numbers are as a percentage of GDP). Gross capital formation (GCF) by the government touched a high of 11.8% in 2021-22, up from 10.7% in 2020-21. This also had a domino effect on private sector investment that jumped from 10% to 10.8% over the same period. In fact, the trends in GCF to gross output ratio or the plough back of funds for creation of fresh capacity shows that for public administration the ratio attained fresh peak in 2021-22 owing to the emphasis on capital expenditure in recent budgets. At the aggregate level, gross capital formation is supposed to have crossed 32% in 2022-23, the highest level since 2018-19.

In 2021-22, gross savings have risen to 30% from 29% in 2020-21. The ratio is supposed to have crossed 31% in 2022-23, the highest since 2018-19. The household savings increased sharply during the pandemic period on account of sharp accretion in financial savings such as deposits. While household financial savings have since then moderated from 15.4% in 2020-21 to 11.1% in 2022-23, savings in physical assets have grown sharply to 11.8% in 2021-22 from 10.7% in 2020-21.

Prima facie, a careful analysis shows that Incremental Capital Output ratio (ICOR), which measures additional unit of capital (investment) needed to produce additional unit of output, has been improving. ICOR which was 7.5 in FY12 is now only 3.5 in FY 22. Clearly, only half of capital is now needed for next unit of output.

Such reducing ICOR in the current years reflects a relative increasing efficiency of capital. The talk on ICOR becomes relevant and shows that the economy is on a sound footing. It is also now clear that potential growth of Indian economy (a global phenomenon) is now lower than earlier. From that point of view, future GDP growth rates even at 7% could still mean a decent number by any standards!

- ◆ India's quarterly sequential Y-o-Y GDP growth has been in a declining trend in FY 23. It has been argued in select quarters that India is going towards Raj Krishna coined rate of Growth (3.5-4%) that predominated the growth in the period of 1947-1980. We find the argument ill-conceived, biased and pre-mature at its best when weighing the numbers against the data on savings and investments.
- ◆ However, it has been observed that institutional share of Public and Private Sector in Total Gross Capital Formation (GCF) has been nearly constant since FY12 at around at around 10 % and 34% of GDP, respectively.
- ◆ Further, share of HouseHold sector in GCF has decreased from 41% in FY 12 to 38% in FY 22. Share of General Government in GCF has increased from 9% in FY 12 to 13% in FY22.



Source: SBI Research

SAVINGS AND INVESTMENT RATIOS

- ◆ The investment and savings data for the past decade reveals interesting points (All numbers are as a percentage of GDP).
- ◆ Gross capital formation by the government touched a high of 11.8% in 2021-22, up from 10.7% in 2020-21. This also had a domino effect on private sector investment that jumped from 10% to 10.8% over the same period. In fact, the trends in GCF to gross output ratio or the plough back of funds for creation of fresh capacity shows that for public administration the ratio attained fresh peak in 2021-22 owing to the emphasis on capital expenditure in recent budgets. At the aggregate level, gross capital formation is supposed to have crossed 32 per cent in 2022-23, the highest level since 2018-19.
- ◆ In 2021-22, gross savings have risen to 30% from 29% in 2020-21. The ratio is supposed to have crossed 31% in 2022-23, the highest since 2018-19. The household savings increased sharply during the pandemic period on account of sharp accretion in financial savings such as deposits. While household financial savings have since then moderated from 15.4% in 2020-21 to 11.1% in 2022-23, savings in physical assets have grown sharply to 11.8% in 2021-22 from 10.7% in 2020-21.
- ◆ **Prima facie, a careful analysis shows that Incremental Capital Output ratio (ICOR), which measures additional unit of capital (investment) needed to produce additional unit of output, has been improving. ICOR which was 7.5 in FY 12 is now only 3.5 in FY 22. Clearly, only half of capital is now needed for next unit of output.**
- ◆ Such reducing ICOR in the current years reflects a relative increasing efficiency of capital. The talk on ICOR becomes relevant shows that the economy is on a sound footing. It is also now clear that potential growth of Indian economy (a global phenomenon) is now lower than earlier. From that point of view, future GDP growth rates even at 7% could still mean a decent number by any standards!

Sector wise Investment to GDP Ratios				
	Public Sector GCF/GDP	Private Sector GCF/GDP	General Government GCF/GDP	Household Sector GCF/GDP
FY12	4.0	13.3	3.5	15.9
FY13	3.8	13.6	3.4	14.7
FY14	3.5	12.9	3.5	12.6
FY15	3.6	13.4	3.5	12.1
FY16	3.9	13.5	3.6	9.6
FY17	3.4	11.6	3.8	10.4
FY18	3.2	11.3	3.6	11.4
FY19	3.7	11.6	3.6	12.2
FY20	3.3	11.0	3.6	11.2
FY21	2.8	10.0	3.8	10.7
FY22	2.8	10.8	4.2	11.8

Source: NSO, SBI Research

Savings and Investment Ratios			
	Gross Savings/GDP	GCF/GDP	GFCF/GDP
FY12	34.6	39.0	34.3
FY13	33.9	38.7	33.4
FY14	32.1	33.8	31.3
FY15	32.2	33.5	30.1
FY16	31.1	32.1	28.7
FY17	31.3	32.0	28.2
FY18	32.1	33.9	28.2
FY19	31.7	33.8	29.5
FY20	29.6	30.4	28.5
FY21	28.8	27.9	27.3
FY22	30.2	31.4	28.9

Source: NSO, SBI Research

Incremental Capital Output Ratio (ICOR)			
	Real GDP Growth%	Investment (GCF) Rate (% of GDP)	ICOR
FY12	5.2	39.0	7.5
FY13	5.5	38.7	7.1
FY14	6.4	33.8	5.3
FY15	7.4	33.5	4.5
FY16	8.0	32.1	4.0
FY17	8.3	32.0	3.9
FY18	6.8	33.9	5.0
FY19	6.5	33.8	5.2
FY20	3.9	30.4	7.8
FY21	-5.8	27.9	-4.8
FY22	9.1	31.4	3.5
FY23	7.0	32*	4.6

Source: SBI Research,* SBI Estimate

Savings to GDP Ratios				
	Public Sector Savings/GDP	Private Sector Savings/GDP	General government Savings/GDP	Household sector Savings/GDP
FY12	3.4	9.5	-1.8	23.6
FY13	3.0	10.0	-1.6	22.5
FY14	2.6	10.7	-1.5	20.3
FY15	2.4	11.7	-1.4	19.6
FY16	2.4	11.9	-1.2	18.0
FY17	2.5	11.5	-0.8	18.1
FY18	2.8	11.2	-1.2	19.3
FY19	2.3	10.5	-1.4	20.3
FY20	3.0	10.2	-2.8	19.1
FY21	2.6	10.5	-6.7	22.4
FY22	2.8	10.4	-2.7	19.7

Source: NSO, SBI Research

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