INDIA'S CURRENT SOVEREIGN RATING – ECONOMY

NEWS: *Despite a sustained fiscal discipline record and narrower fiscal deficit, international rating agencies such as Moody's and Fitch are hesitant when it comes to upgrading India's sovereign rating.*

WHAT'S IN THE NEWS?

- **Fitch Ratings has assigned India a "BBB-" rating with a stable outlook.**
    - Fitch Ratings is one of the top three global credit rating agencies that assess a country's financial health and ability to repay debts.
    - "BBB-" is the lowest investment-grade rating, meaning that India's economy is stable, but risks exist.
    - A **stable outlook** means that the rating is unlikely to change in the near future unless major economic conditions shift.
- **This indicates good credit quality with low default risk, but economic downturns can affect it.**
    - A "BBB-" rating suggests that India is **financially reliable and unlikely to default** on its debt payments.
    - However, if economic conditions deteriorate, such as **slow growth, fiscal mismanagement, or rising inflation**, the country's ability to meet its financial obligations could weaken.
- **"BBB-" is the lowest investment-grade rating, meaning India barely qualifies for investment-grade borrowing.**
    - Investment-grade ratings signal that a country is **safe for investors** and has a **low risk of defaulting**.
    - Since "BBB-" is the lowest grade in this category, any downgrade would push India into **junk bond status**, making borrowing more expensive.
- **Other agencies have similar ratings:**
    - **Moody's:** Rated India **Baa3**, which is the lowest investment-grade level in Moody's system.
    - **S&P (Standard & Poor's):** Rated India **BBB-**, same as Fitch.
- **Comparison with Other Countries:**
    - **China:** Rated **A+**, meaning its economy has **higher creditworthiness** and a **much lower risk of default** than India.
    - **USA:** Rated **AA+**, indicating an **extremely low risk of default**, making it one of the safest economies for investors.

Sovereign Credit Rating (SCR):

- SCR is **an independent assessment of the creditworthiness of a country or sovereign entity.**
- It can **give investors insights into the level of risk associated with investing in the debt of a particular country,** including any political risk.
- In addition to issuing bonds in external debt markets, another common motivation for countries to obtain a sovereign credit rating is **to attract Foreign Direct Investment (FDI).**
- At the request of the country, a credit rating agency will evaluate its economic and political environment to assign it a rating.

        - Moody's considers a Baa3 or higher rating to be of investment grade, and a rating of Ba1 and below is speculative.
        - S&P gives a BBB- or higher rating to countries it considers investment grade, and grades of BB+ or lower are deemed to be speculative or "junk" grade.

India's Fiscal Performance

- **The Union Government has focused on fiscal consolidation to improve its financial health.**
    - **Fiscal consolidation** means **reducing budget deficits and government debt** to ensure a more stable economy.
    - The government has taken several measures to **reduce unnecessary spending and increase revenue** to strengthen India's financial position.
- **Key Measures Taken:**
    - **Increased capital expenditure, improving long-term economic growth prospects.**
        - The government is investing in **infrastructure projects** like roads, railways, and power generation, which can boost economic growth and productivity.
    - **Better targeting of subsidies and cutting wasteful spending, reducing unnecessary expenses.**
        - Instead of blanket subsidies, the government is ensuring that **only the needy receive financial support**, preventing misuse of funds.
    - **Better revenue mobilization to reduce reliance on borrowing.**
        - India has improved tax collection through **GST (Goods & Services Tax), income tax reforms, and digital tracking**, reducing the need for excessive borrowing.
- **Fiscal Deficit Reduction:**
    - **FY21: 9.2% of GDP** – The fiscal deficit was extremely high due to **COVID-19 relief measures and reduced revenues.**
    - **FY25: 4.8% of GDP** – The deficit has been **almost halved**, indicating better fiscal management.
    - **FY26 Projection: 4.4% of GDP** – The government is planning **further reductions** to improve financial stability.
- **Government Debt Reduction Targets:**
    - **FY25: 57.1% of GDP** – The government aims to **bring down debt levels gradually**.

- **FY31 Target: 50% of GDP** – The long-term goal is to **align with international benchmarks and strengthen investor confidence.**

Large emerging economies are yet to break into the top league.

Country	Sovereign rating*	Credit quality
Australia	AAA	Highest
USA	**AA+**	**High**
China	A+	High
India	**BBB-**	**Good**
Brazil	BB	Speculative
South Africa	**BB-**	**Speculative**

*latest sovereign rating by Fitch

Source: Mint research

Concerns of Rating Agencies

- **Despite acknowledging India's fiscal discipline and deficit reduction, agencies demand further improvements.**
    - While rating agencies have **recognized India's progress**, they **expect further reductions in government debt and fiscal deficit** before considering a rating upgrade.
- **Key concerns for a rating upgrade:**

1. **High Government Debt**
    - India's **total government debt exceeds 80% of GDP**, meaning the government owes a large amount compared to the economy's size.
    - **BBB-rated peer countries** have an **average government debt of 50% of GDP**, making India's debt appear too high.
2. **High Interest Burden**
    - The government **spends 25% of its revenue just on interest payments**, leaving less room for **development projects and public welfare.**
    - In contrast, **BBB-rated countries spend only 8% of their revenue on interest payments.**
3. **Need for Stronger Revenue Mobilization**
    - Rating agencies want India to **increase its tax revenues** by expanding the tax base, reducing evasion, and enhancing compliance.

Are Rating Agencies Biased Against India?

- **Some experts, including UN Trade and Development, question possible bias in rating methodologies.**
    - Many analysts believe that **global rating agencies apply stricter standards to emerging economies** like India, while developed nations receive more favorable ratings.
- **India's Economic Strengths vs. Rating Stagnation:**
    - Despite strong economic growth, India's sovereign rating **has remained unchanged for two decades.**
    - **Economic Growth:**

    - India has become the **5th largest economy**, overtaking the UK and France.
    - It remains the **fastest-growing large economy** in the world.
- **Strong Foreign Reserves:**
    - India holds **sufficient foreign exchange reserves**, ensuring stability in **import payments and external debts.**
- **Robust Financial System:**
    - India's **banking system, stock market, and corporate sector remain resilient** and attract **strong foreign investment.**
- Despite all this, **India's credit rating has remained at BBB-, leading to concerns about unfair assessment.**

Importance of a Rating Upgrade

- **A higher credit rating has major economic benefits:**
    1. **Lower Borrowing Costs**
        - A better rating means India will **pay lower interest rates on loans**, making borrowing **cheaper for both the government and businesses.**
    2. **Boosts Foreign Investment**
        - Investors prefer **higher-rated economies**, so an upgrade would bring **more foreign direct investment (FDI)** into India.
    3. **Stronger Economic Growth**
        - Lower borrowing costs and increased investment can **fuel infrastructure development and job creation**, boosting GDP growth.
    4. **Higher Credibility in Global Markets**
        - A rating upgrade enhances India's **reputation as a stable economy**, making it more **attractive for global investors.**

Conclusion

- **India has made significant progress in fiscal discipline and economic growth, but sovereign ratings have remained unchanged for decades.**
- **Key areas of improvement for a rating upgrade include:**
    - **Reducing government debt** closer to **50% of GDP**.
    - **Lowering interest burden** on government revenues.
    - **Enhancing tax collection and revenue mobilization.**
- **A higher credit rating can accelerate India's economic momentum, making it a more attractive investment hub globally.**

Source: https://www.livemint.com/economy/mint-primer-sovereign-rating-how-india-can-go-from-b-to-a-11738683859458.html#:~:text=By%20better%20targeting%20subsidies%20and,further%20to%204.4%25%20in%20FY26.