



Moody's rating upgrade – Impact on India's economy

Description

Background :-

On 16th November 2017, international rating agency, 'Moody's Investor Services' upgraded India's government debt rating from Baa3 to Baa2 after 13 years and also changed the outlook from 'stable' to 'positive'. This upgrade will boost the Indian economy by reducing the cost of overseas borrowing and improve the investments in India.

What were the major reasons behind the upgrade?

The agency's decision was based on the positive outlook of the economic and institutional reforms which will create high growth possibilities and decrease the government debt. An article in Business Today stated the reasons given by Moody's for this upgrade in four points which are as follows:

- **Improved Business climate** : The report stated that economic reforms including GST, demonetisation, Aadhaar and the Direct Benefit Transfer will improve the business climate by reducing informality and hence foster strong and sustainable growth. The effect of certain reforms like GST and demonetization will be realised in the future. It also expected the real GDP growth to moderate to 6.7% in the fiscal year ending in March 2018 (FY2017).
- **Stable public indebtedness** : The report highlighted that the recent reforms will create more confidence that the high level of public indebtedness will remain stable even in the event of shocks and will ultimately decline.
- **Strengthened institutions due to structural reforms** : Government's efforts to reduce corruption and improve tax collection will lead to formalising of the economy and will lead to the strengthening of the Indian institutions. Also the adoption of new Fiscal Responsibility and Budget Management (FRBM) and the formation of Monetary Policy Committee (MPC) will improve the fiscal and the monetary policy respectively.

- **Government support to banks:** The agency said that the comprehensive recapitalization of the Public Sector Banks is an active step towards the resolution of the NPA's and the banking losses. The agency also held the Insolvency and Bankruptcy Code as useful in addressing the key weakness in India's sovereign credit profile.

How will the upgrade boost Indian economy?

This decision will impact the Indian economy in various ways; some of them are as follows:

- The decision will induce fresh round of portfolio investments and reduce the cost of external commercial borrowings.
- The gap between China and India will reduce. However China is at A1 and India is still behind but India can boast of reducing the gap on the basis of its own merits rather than other country's demerits.
- Moody's decision reflects that agencies throughout the world recognise India's improvement through institutional changes and maintained fiscal discipline.
- The upgrade places India at an upper level as compared to other Baa rated countries. This indicates higher growth potential.
- The rating grew 108% from 2006 to 2016, as compared to 74% for Baa-rated median. This definitely indicated remarkable improvement.

The upgrade comes with a warning:

Moody's noted in its report that "The rating could also face downward pressure if the health of the banking system deteriorated significantly or external vulnerability increased sharply." This brings up the need to maintain the Indian fiscal metrics to avoid a downgrade.

Conclusion:

Not only the upgrade instils confidence in investors in India but also provides an international recognition to the country. Thus it can be understood that the upgrade will boost the Indian economy.

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