India's Credit Ratings: Boost to Investors' Sentiment

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India's macroeconomic health, particularly its investment position and debt indicators (economic growth, current account balance, FDI inflows, and forex reserves) have improved since 2013. India has clearly demonstrated its ability to repay its debt and always exhibited remarkably high willingness to pay; it has never defaulted on its obligations. India has the capacity to bear large debt and can simultaneously secure financing to remain solvent. It is stable, and is one of the fastest growing economies worldwide, and this reflects in positive investor sentiment over the past few years

Earlier this year, Economic Survey 2016-17 pointed out the bias in perception about Indian economy by international Credit Rating Agencies (CRAs). On the backdrop of the debate whether India's credit ratings deserve an upgrade or not, the Moody's has finally upgraded India's ratings from BAA3 to BAA2 and outlook from positive to stable. This upgrade has come after a gap of more than thirteen years. The Moody's have cited various reasons for this upgrade, viz. change in taxation regime with the introduction of Goods and Services Tax (GST), Insolvency and Bankruptcy Code to resolve bankrupt cases, institutional reforms in the form of India's aggressive stance for a less cash economy, raising the Foreign Direct Investment (FDI) equity limits on various sectors, emphasis on infrastructure development with various new projects being announced to enhance India's road and port network and following the fiscal consolidation path. This is the second positive news about Indian economy after it was ranked 100 in the World Bank's Ease of Doing Business indicators by moving up 30 places in one year. On the contrary, another agency, the Standard and Poor' (S&P) did not upgrade credit ratings for India despite notable improvements in the overall health of the Indian economy in the last few years. Infact, S & P has continued to assign a stable rating for India since 2007.

Importance of Credit Ratings

CRA, in order to rate investments, consider broad financial, macroeconomic, and stability indicators in a borrower country and its economic outlook to estimate its ability and willingness to pay its debt (and its likelihood of default). Three international CRAs regulate most of the world market—Standard and Poor's (S&P), Moody's, and Fitch—and maintain that a credit rating should not be intended as a guarantee of credit quality, as the future cannot be forecast accurately and ratings should be considered just a market signal. Also, different CRAs do not measure similar things before taking decisions on credit ratings. In particular, S&P is most interested in the creditworthiness of the borrowers, i.e. the probability of default. Moody's, on the other side, examines the expected losses which are a part of the broader likelihood of default. Though the credibility of ratings agencies has moderated during post financial crisis where AAA rated investments defaulted, their importance has by no means diminished. Credit ratings do not use a rule-based method, and are subjective, but these affect the cost of borrowing and access to international capital markets and so remain important, and

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