India outlook is stable, but fiscal deficit a key constraint on ratings

Global ratings agency Moody's accords a Baa3 rating for India's sovereign debt, with a positive outlook. The agency's vice-president and senior analyst, sovereign risk group, Atsi Sheth, spoke to Arup Roychoudhury of FE on the sidelines of the ADB Summit in Greater Noida:

Moody's is perceived to be more positive on India compared with other rating agencies. What is it about the India story that you have factored in and maybe other agencies have not?

Our outlook on India's rating is stable. Nothing that has happened over the last one year, or is likely to happen over the next 12-18 months is likely to change the default risk of the sovereign. We focused on whether the downturn has (stopped) and the probability of the government being able to repay its debt.

The Cabinet Committee on Investment has cleared certain projects. The next step is those projects actually getting off the ground. There has been movement in the right direction. It has not gone as far as to actually yield growth. The fiscal deficit is a key constraint on India's ratings. The government did revise its forecast and met that forecast by controlling expenditures. So we have seen actions following policy announcements, but the fiscal deficit is still much higher than other countries rated at the same level. What has happened in the past six months is certainly a positive, but it has not changed the credit profile.

Can you give us a sense of what India needs to do to warrant a positive outlook and realistically, how long will it take to get there?

We have a stable outlook on the rating at this point because we don't see at this point a positive momentum in the ratings over the next 12-18 months. If the country's fiscal deficit and the high level of government debt are brought down, to levels that are comparable to other countries in the same ratings range, that would be a positive. The other constraint is that India, in the last few decades, has been susceptible to inflationary pressures. We think that even as growth remains at 5 percent or higher, inflationary pressures will be recurring. If we found movement in agriculture productivity to address food inflation, if we saw movement in terms of infrastructure, that addresses bottlenecks, that would warrant a positive outlook.

How do you think India can deal with the problems it faces in infrastructure projects' implementation and completion?

One way of looking at it is by seeing where there has been progress, and what led to that progress. That gives you a clue as to what works in the Indian context. There has been development in pockets. In these pockets, policy did not impede output, financing was available and the private sector participation was profitable. Those are the conditions we need to replicate elsewhere. These conditions are not easy, but they are not impossible as well.

How much of India's economic growth do you see coming from the rural sector?

Moody's has always looked at the data on consumption in India, and that data tells you that rural consumption is very important in India. It does move growth. It has been a driver of growth for a long time. What's interesting is that manufacturing is now spreading into rural areas. What is thought of as rural is no longer simply people employed in agriculture. People live in a village, and work in a factory, or a mine. So the definition of rural in India has changed. That is going to be a driver of growth in the future because it is manufacturing that will create the jobs, it is infrastructure that will create the growth potential. All of that will happen in both rural and urban areas.

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