India's Rating Upgrade: Momentum vs. Durability in Emerging Market Assessment

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Executive Summary

Credit ratings can look like dry technical opinion, but in emerging markets such as India they have a power that extends far beyond the figures. One upgrade or downgrade can have shock waves spreading through bond markets, foreign investment flows, and even fiscal projections. The recent action by S&P to raise India's sovereign rating has again put the focus on the nation's economic path but with a difference. In contrast to S&P, Moody's and Fitch are still holding back their upgrades, leaving investors wondering: what do these differences actually mean?

This article examines that question in historical and statistical context. It links previous rating changes to significant economic cycles, demonstrating how reforms, inflation containment, and fiscal consolidation have always influenced the opinions of agencies worldwide. It also reflects on what that divergence has come to mean for India's credibility now, and how it might shape government policy as well as investor perceptions in the coming years.

At risk is more than a grade. It is whether India's growth momentum and fiscal commitments are perceived as sustainable, and whether the world accepts the story the numbers are telling.

Chapter 1: Introduction

"Sovereign credit ratings serve as critical market barometers, reflecting a nation's perceived risk, fiscal credibility, and resilience to policy shocks, thereby significantly influencing global capital flows and investment appetite."

Standard &Poor (S&P) Global Ratings recently upgraded India's sovereign credit rating from **BBB– to BBB**, marking a significant moment for the country's financial and economic positioning (the hierarchy of the ratings are provided in the annexure). The move is especially noteworthy as it comes at a time when many emerging economies are grappling with downgrades, fragile fiscal balances, and global uncertainty. While Moody's and Fitch have maintained their outlooks unchanged, S&P's decision signals a differentiated vote of confidence in India's trajectory.

Sovereign credit ratings function as the financial markets' primary assessment tool for evaluating a country's economic stability and government reliability. When rating agencies like Moody's, S&P, or Fitch adjust a nation's credit score, they're essentially providing a professional judgment on that country's ability to honor its debt obligations and maintain sound economic policies. These ratings directly impact how much foreign investors are willing to invest in a country and at what cost. A higher rating translates to lower borrowing costs for both government and corporate entities, while also attracting more institutional investment. Markets treat these ratings as shorthand for investment safety; they influence everything from bond yields to currency strength and foreign direct investment flows.

Beyond their signaling function, sovereign credit ratings also mitigate information asymmetries between borrowers and lenders. By providing a standardized benchmark of credibility, they reduce uncertainty in capital allocation decisions and thereby improve access to international finance. This enhanced credibility contributes to more favorable borrowing conditions and catalyzes financial system development, a process widely regarded as integral to sustained economic growth. Furthermore, the structural linkage between sovereign and corporate ratings often referred to as the sovereign ceiling effect means that the national rating directly constrains the ratings of domestic firms. Consequently, improvements in sovereign creditworthiness not only benefit governments but also expand financing opportunities for the private sector, reinforcing financial deepening and broader economic development.[1]

These ratings condense complex macroeconomic and political landscapes into easily digestible metrics, guiding international investors and financial institutions in their portfolio allocation decisions. Essentially, a sovereign rating quantifies the probability of a country defaulting on its debt obligations, a perception that cascades down to the corporate level as well. The demand for sovereign credit ratings has increased dramatically as more governments and companies in riskier countries borrow in international markets.

Against this backdrop, India's credit upgrade cannot be viewed in isolation; it reflects the interplay of macroeconomic stability, reforms, and resilience that have defined the country's recent journey. This country has shown robust economic momentum, with a significant growth rate in 2023, positioning it to become a major global economy. This growth is supported by a burgeoning middle class and progressive regulations (Kumar & Maiti, 2024). The steady push for internationalization of the rupee has enhanced India's financial credibility and reduced its vulnerability to external shocks. At the same time, policies focused on inclusive growth have strengthened domestic demand and created a broader consumption base that cushions the economy in times of external stress. Fiscal space has also been reinforced through prudent monetary–fiscal coordination, such as the calibrated transfer of central bank surpluses, which has supported public spending without undermining fiscal discipline. These factors collectively create a stable macroeconomic foundation, explaining the rationale behind the upgrade. The Indian economy has demonstrated resilience even when facing global challenges. For instance, during the global financial crisis, while some financial markets and trade flows were affected, India's banks largely remained unaffected in the initial phase, showcasing a degree of resilience (Kumar & Vashisht, 2009). Factors such as crude oil prices, economic policy uncertainty, exchange rates, and foreign institutional investment significantly influence India's sectoral indices (Chauhan et al., 2025). Global interest rates are influenced by a principal component across major developed and developing economies, including

[1] https://www.sciencedirect.com/science/article/pii/S1042443125000435#b18

India, which can impact investment and growth ("Gulf Cooperation Council: Pursuing Visions Amid Geopolitical Turbulence," 2024; Ratti & Vespignani, 2015).

Despite the global financial crisis leading to a major realignment of sovereign ratings, particularly affecting advanced economies, large developing economies like India have experienced minor erosions or even sustained their ratings and outlooks (Basu et al., 2013). This relative stability or occasional upgrade, amidst a period where highly rated economies faced downgrades, has made countries like India relatively more attractive to capital flows. Macroeconomic factors such as high GDP growth, rising foreign reserves, declining fiscal deficits, and increasing exports have been considered in the upgrading of India's sovereign rating. The stock market in India has also shown statistically significant responses to revisions in India's sovereign credit rating announcements (Kumar, 2001). This performance, in a landscape of global uncertainty, contributes to placing India in a "select few" category.

Such relative resilience in India's sovereign credit profile does not just shape macroeconomic narratives, it has tangible consequences for businesses operating within the country. Sovereign ratings cascade down to the corporate level, influencing how companies access international capital, how investors perceive domestic markets, and ultimately, how firms plan their growth strategies. Sovereign credit ratings are crucial for corporate leaders due to their direct influence on borrowing costs, market mood, and international investor sentiment.

- **Borrowing Cost:** Sovereign ratings are a key determinant of the interest rates a country faces in international financial markets, directly impacting its borrowing costs (Afonso et al., 2007). A country's sovereign rating can act as a "ceiling" or constraint for the credit ratings assigned to corporations operating within that country (Ntsalaze et al., 2017). If a sovereign is poorly rated, companies within that country may face limitations in securing investor funding at competitive rates from international financial market. Conversely, better sovereign ratings can facilitate external borrowing at favorable interest rates for the country, fostering a more conducive environment for corporate financing (Samantaraya & Verrier, 2009). There is evidence that high sovereign risks can persistently increase private sector borrowing costs in emerging markets (Li et al., 2022), and the corporate sector can face higher borrowing costs when the public sector's external debt is higher (Ağca & Celasun, 2012).

- **Market Mood & International Investor Sentiment:** Sovereign rating announcements can lead to significant responses in the stock market, indicating their influence on market mood. The dispersion of credit information through sovereign ratings contributes to the stability of financial markets and informs market investors (Li et al., 2019). This means a positive sovereign rating outlook, or an upgrade, can instill greater confidence among both domestic and international investors, potentially leading to increased capital inflows, including foreign direct investment, as sovereign credit ratings are important drivers of these flows (Cai et al., 2018).

Against the background of this evolving landscape of global perception, India's rating upgrade is simultaneously validation and omen. It confirms the resilience of an economy that has managed to stay steady despite fluctuations of external volatility, even as it indicates the promise of deeper reforms, fiscal discipline, and sustained growth. The world is intently watching policymakers, investors, and businesses equally so because sovereign ratings, technical in nature though they are, possess immense emotional weight in scripting narratives of trust and stability.

For India, this is less a destination and more a threshold. The upgrade signals the success that has been accomplished. But it also shines a light on the reforms that are still awaiting completion. In the chapters that follow, we will follow this path, looking at how credibility is forged, how confidence is tested, and how the relationship between markets and policy will determine if the optimism of today is convertible into the momentum of tomorrow.

Chapter 2: Comparison among S&P, Moody's, Fitch Ratings

S&P has upgraded India's long-term Sovereign Credit Rating to 'BBB' from 'BBB-' and short-term rating to 'A-2' from 'A-3' with a Stable Outlook. This is the first upgrade of India's sovereign rating by S&P since 2007, when it had upgraded the nation to investment grade at BBB-. Fitch has rated India 'BBB-' since 2006, and Moody's has been at 'Baa3' since June 2020 (the complete rating history of India is provided in the annexure).

Table 1: Sovereign credit ratings history of India

Agency	Rating	Outlook	Date
Standard & Poor's	BBB	Stable	8/2025
Fitch	BBB-	Stable	8/2024
Standard & Poor's	BBB-	Positive	5/2024
Fitch	BBB-	Stable	1/2024
Moody's	Baa3	Stable	8/2023
Fitch	BBB-	Stable	5/2023
Fitch	BBB-	Stable	12/2022
Fitch	BBB-	Stable	6/2022
Fitch	BBB-	Negative	11/2021
Moody's	Baa3	Stable	10/2021
Fitch	BBB-	Negative	4/2021
Moody's	Baa3	Negative	6/2020
Fitch	BBB-	Negative	6/2020

Source

The upgrade follows S&P's May 2024 upgrade of India's outlook to positive from stable, based on robust growth and enhanced quality of government spending. India is rated BBB, just like Greece, Mexico, and Indonesia. At the top ratings, rated AAA, are advanced economies like Australia, Canada, Denmark, and Germany. Surprisingly, the richest countries do not necessarily have the top ratings. For example, the United States saw a downgrade from AA+ by S&P in 2011, thereby ending its AAA run on the back of rising debt concerns.

2.1. Methodological Differences

When assessing sovereign creditworthiness, S&P Global, Moody's, and Fitch all weigh fiscal health, growth prospects, inflation stability, and institutional strength. Yet, the **differences lie in how they translate these fundamentals into rating outcomes**. Each agency's framework reflects a distinct balance between near-term numbers and long-term credibility, which explains why their responses to India's recent fiscal and macroeconomic improvements have not been uniform.

2.1.1. Speed of Incorporation

- **S&P Global:** Uses a structured scoring framework with five pillars (institutional, economic, external, fiscal, and monetary). Each is rated on a 1–6 scale and combined into profiles. Because the framework is ratio-driven and forward-looking, improvements in fiscal deficits, debt ratios, growth, or inflation feed directly into the scores. The methodology explicitly incorporates projections of GDP, inflation, and fiscal balance, which makes S&P quicker to respond when a government presents and begins to deliver on a consolidation path.
- **Moody's:** Places more weight on durability over time. Even if recent indicators improve, Moody's holds back until evidence shows that improvements are sustainable across cycles. Its event-risk "minimum function" means that a single weak area (e.g., external vulnerability, banking sector stress) can cap the overall rating. This makes upgrades slower.
- **Fitch:** Runs a Sovereign Rating Model (SRM) that captures data on growth, inflation, fiscal balance, reserves, etc. But the Qualitative Overlay (QO) can adjust the model outcome by up to ±2 notches (capped at ±3). This overlay moderates abrupt shifts, meaning Fitch rarely reacts to short-term improvements without longer-term confirmation.

2.1.2. Fiscal Discipline vs. Fiscal Credibility

- **S&P Global:** Fiscal ratios are central — general government debt/GDP, interest/revenue ratios, and fiscal deficit trajectories carry significant weight. If debt affordability improves (e.g., through stronger nominal GDP or lower inflation), the fiscal score strengthens. Importantly, S&P accepts credible medium-term government projections (such as India's glide path from 9.2% deficit to ~4.4%) as part of its assessment, provided they align with recent performance. Thus, it rewards headline consolidation efforts more quickly than others.
- **Moody's:** Focuses less on headline ratios and more on credibility of fiscal institutions. It asks whether revenue systems are reliable, subsidies and contingent liabilities manageable, and buffers being rebuilt. For Moody's, numbers alone are insufficient; what matters is whether fiscal improvements are structurally sustainable and institutionally enforceable.
- **Fitch:** Includes fiscal balance, debt/GDP, and interest/revenue in its SRM, but evaluates them alongside financing flexibility and contingent liabilities. A country may show improving fiscal ratios, but Fitch tempers upgrades if rollover risks, state-owned enterprise liabilities, or weak revenue bases persist.

2.1.3. Growth and Inflation Sensitivity

- **S&P Global:** Growth and inflation feed directly into debt sustainability metrics. Strong nominal GDP growth reduces debt/GDP, and lower inflation improves monetary credibility and debt affordability. Since the methodology is forward-looking, even projected improvements (e.g., growth above peers, inflation trending down) influence scores immediately. This responsiveness makes S&P particularly sensitive to India's combination of robust growth and sharply lower inflation.
- **Moody's:** Growth is assessed for long-term sustainability and resilience to shocks, not short bursts. Inflation is not judged on a single print; Moody's looks for evidence that monetary institutions can maintain low, predictable inflation across cycles. This emphasis on consistency makes Moody's less responsive to India's short-term disinflation.
- **Fitch:** Growth and inflation are explicit SRM inputs, but the model output can be moderated by the overlay. Even if GDP growth is strong and inflation falls, Fitch may not upgrade unless broader structural weaknesses (in governance, banking, or external balances) improve simultaneously.

2.1.4. Risk and Stability Lens

- **S&P Global:** The framework gives primacy to solvency and liquidity metrics. Adjustments can be made for extraordinary risks (political, external, contingent liabilities), but absent such shocks, improving ratios dominate. Thus, if fiscal and inflation numbers strengthen, the rating can rise despite lingering risks.
- **Moody's:** The event-risk factor uses a minimum function, meaning one area of weakness (e.g., political risk, financial sector fragility, external vulnerability) can cap the entire rating. This conservative approach slows upgrades, as India still faces vulnerabilities in banking and external accounts.
- **Fitch:** The Qualitative Overlay ensures a cautious adjustment path. Even when quantitative indicators improve, risks in governance, external finance, or public sector liabilities prevent quick rating moves. Fitch favors stability and avoids sudden upgrades unless vulnerabilities are clearly resolved.

Table 2: Comparison among methodologies of S&P, Moody's and Fitch

DIMENSION	S&P GLOBAL	MOODY'S	FITCH
INCORPORATION SPEED	Forward-looking, ratio-driven; projections built in, so ratings move quickly with recent fiscal/monetary shifts.	Slow; prioritizes durability, with event-risk "minimum function" capping ratings.	SRM captures improvements but QO overlay restrains sudden changes.
FISCAL ASSESSMENT	Heavy weight on debt/GDP, interest/revenue, deficit trajectory; rewards credible medium-term plans.	Focuses on fiscal credibility and buffers; numbers alone insufficient.	Fiscal ratios included but balanced against financing flexibility and contingent liabilities.
GROWTH SENSITIVITY	Growth & inflation directly feed debt sustainability; projections influence scores.	Long-term growth sustainability emphasized; inflation judged on consistency across cycles.	Growth & inflation explicit inputs but moderated by overlay, limiting quick upgrades.
RISK LENS	Solvency/liquidity metrics dominate unless extraordinary risks force adjustment.	Event-risk factor caps rating if any area is weak.	Overlay ensures conservative changes; avoids abrupt rating shifts.

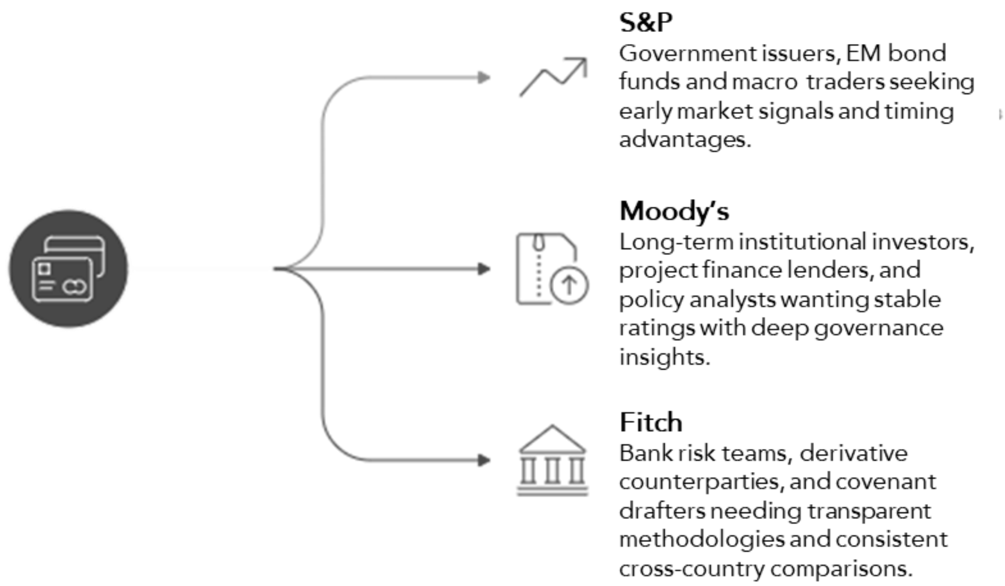
Source: S&P, Moody's, Fitch

In practice, this divergence means that S&P Global's forward-looking, ratio-based framework was primed to reward India's recent fiscal consolidation, declining debt trajectory, and sharp disinflation. By contrast, Moody's and Fitch have held back, as their methodologies place greater weight on institutional durability, structural vulnerabilities, and the need for consistency across multiple cycles. These methodological contrasts are central to explaining why only S&P Global has upgraded India's rating at this stage, while the others continue to wait for further confirmation.

2.2. Relevance of Each of It

The upgrade by S&P Global can be understood as a natural outcome of the agency's forward-looking methodology, which translates improvements in fiscal ratios, growth momentum, and inflation management into rating action more swiftly than its peers. India's fiscal trajectory, marked by aggressive consolidation since the pandemic, a credible medium-term deficit path, and a declining debt burden, has directly strengthened its fiscal profile in S&P's assessment. When coupled with sustained high growth relative to global peers and an easing inflation environment that reinforces monetary credibility, the case for an upgrade aligns clearly with the way S&P interprets sovereign resilience and debt sustainability. Based on their different methodology of rating, there can be different types of people who will be largely focusing on the respective ratings to gain the most amount of benefit.

Beneficiaries of Each Ratings



2.2.1. S&P Global: Forward-Looking Responsiveness

S&P's model is characterized by its extensive use of forward-looking external, fiscal, and monetary ratios. Its rating system incorporates GDP growth, fiscal deficit, and inflation forecasts into its scoring, rendering ratings highly sensitive to recent and future developments. S&P's sensitivity is most favorable to sovereign debt managers and quasi-sovereign issuers wanting to benefit from periods when fundamentals are consolidating by accessing international markets at reduced costs. Being able to spot early signs of consolidation efforts, such as India's post-pandemic fiscal glide path, has the power to significantly lower spreads and borrowing costs as soon as its effect is felt in S&P's ratings.

For short- to medium-term investors, including investors in emerging-market bond funds, hedge funds, and currency trading, S&P's approach provides a useful indicator of macroeconomic inflection points. Since upgrades are also incorporated in ratings more promptly, market participants who act quickly in response to these indications are well-positioned to capture rewards. However, in this sense, S&P's approach is appropriate for those who prioritize speed and market timing rather than long-term consistency.

2.2.2. Moody's: Durability and Institutional Confidence

Moody's ratings are intended to reflect not just quantitative progress but also the credibility and durability of such progress. By design, Moody's event-risk approach employs a "minimum function," that is, a deviation in one dimension or another, whether political stability, banking system depth, or external buffers, can cap the overall rating. This makes Moody's less sensitive to outstanding fiscal or inflation successes; however, its ratings are more meaningful as a signal of long-term resilience.

This design makes Moody's ratings of greatest worth to long-term institutional investors like pension funds, sovereign wealth funds, and insurance companies, who care most about reducing rating volatility in their portfolios. It also makes it suitable for policy analysts, development banks, and ESG-conscious investors, who care less about tactical gains and more about structural reforms, good governance, and policy credibility. For these participants, Moody's conservatism is not a flaw but a protection: it prevents rating upgrades to be based on cyclical improvement rather than systemic strength and is therefore a better guide for capital invested over decades.

2.2.3. Fitch: Transparency and Risk Management

Fitch uses a quantitative Sovereign Rating Model (SRM) and a bounded Qualitative Overlay (QO). The SRM relies on explicit, publicly available inputs (e.g., debt-to-GDP, interest-to-revenue shares, reserve coverage, and current account balances). The QO, on the other hand, allows for adjustments within pre-specifiable ranges (±2 notches per pillar and ±3 overall). This approach yields a greater degree of comparability and predictability, particularly where ratings are used in financial contracts. The most critical users of Fitch's approach are treasury desks, risk managers, and lenders who require ratings to be directly mapped to internal risk systems and utilized as objective triggers in derivative contracts or bond covenants. Because Fitch makes publicly available inputs and limits of adjustments, its ratings are audit-proof to some extent and thus avoid rating shocks having uncontrolled financial effects. In addition, Fitch's approach aids cross-country benchmarking, and thus it is a bank, analyst, and multilateral institution favorite for cross-jurisdiction sovereign risk assessment.

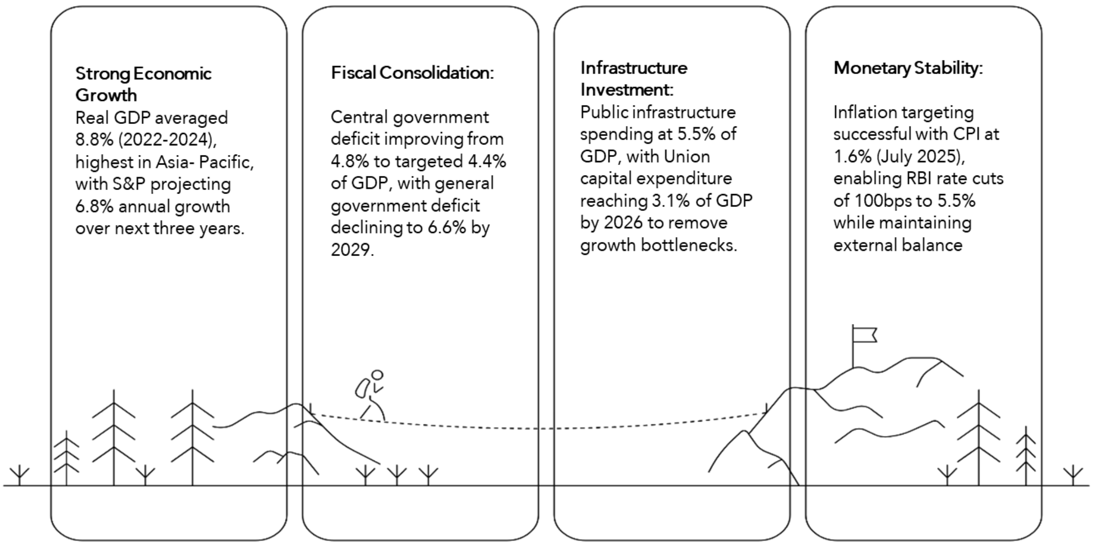
Taken together, these improvements explain why S&P Global has moved ahead of its counterparts in revising India’s rating upward. The agency’s framework is designed to recognize momentum in fiscal and macroeconomic performance, rewarding governments that demonstrate credible progress even before such progress has fully matured. This stands in contrast to Moody’s and Fitch, whose methodologies place greater weight on structural durability, institutional depth, and risk containment. The divergence now evident between S&P’s rating and those of the other two agencies therefore reflects not a contradiction, but a methodological difference that sets the stage for understanding the underlying reasons behind India’s upgrade and the caution shown elsewhere.

Chapter 3: Operation of Sovereign ratings and Reason behind the Update in India's rating by S&P

3.1. India's Current Economic Outlook

India's economy has demonstrated remarkable resilience and dynamism in recent years, underpinned by robust growth, targeted fiscal reforms, and strategic policy interventions. Real GDP growth averaged 8.8% between fiscal 2022 and 2024, the highest in the Asia-Pacific region, while medium-term projections remain strong at 6.8% annually over the next three years. At the same time, the government has strengthened fiscal discipline, gradually reduced deficits and improving debt management, even while financing significant infrastructure investments. Complementing this, monetary policy reforms, particularly inflation targeting, have stabilized price expectations, and India's external position remains solid. Collectively, these developments reflect a forward-looking economic trajectory that reinforces the country's credibility in the eyes of international investors.

India's Recent Macroeconomic Improvements



3.1.1. Economic Growth

- Real GDP growth averaged 8.8% between fiscal 2022 and 2024, the highest in the Asia-Pacific region.
- S&P projects annual GDP growth of 6.8% over the next three years, supporting a moderation in the government debt-to-GDP ratio.
- Robust economic expansion is improving India's credit metrics, providing a solid foundation for sustained growth over the next 2–3 years.

3.1.2. Fiscal Discipline

- The Indian government is following a clear and gradual path towards fiscal consolidation, strengthening economic stability and credibility.
- Central government fiscal deficit: 4.8% of GDP in fiscal 2025 (provisional), targeted at 4.4% for fiscal 2026.
- State government deficits: expected to average 2.7% of GDP over the next 3–4 years.
- General government deficit: projected to decline from 7.3% of GDP in fiscal 2026 to 6.6% by fiscal 2029.
- Net debt growth: estimated at 7.8% of GDP, improved from 9–13% during the pandemic years.
- Large infrastructure investments have been funded without significantly widening the current account deficit, reinforcing fiscal credibility.

3.1.3. Infrastructure & Investment

- Government spending quality has improved, with a strong focus on infrastructure investment.
- Union government capital expenditure is expected to reach INR 11.2 trillion (3.1% of GDP) by fiscal 2026.
- Total public investment in infrastructure, including state governments, is estimated at around 5.5% of GDP, matching or exceeding many peer countries.
- These investments in infrastructure and connectivity are expected to remove bottlenecks that previously limited long-term economic growth.

3.1.4. Monetary & External Stability

- Monetary policy reforms, particularly the shift to inflation targeting, have stabilized price expectations.
- Consumer price index (CPI) growth has averaged 5.5% over the past three years, staying within the RBI's 2–6% target band.
- Recent CPI inflation has fallen to 1.6% in July 2025, down from 2.1% in June.
- With inflationary pressures contained, the RBI began monetary easing in February 2025, cutting the policy repo rate by 100 basis points to 5.5%.
- External position: India maintains a modest net external asset balance, with small current account deficits supported by stable domestic demand and a moderately weaker rupee, which enhances export competitiveness.

These recent economic improvements in India, triggers S&P's credit rating to the country.

3.2. Mapping India's Economic Improvements to S&P's Rating Change

S&P's decision to upgrade India's sovereign rating from **'BBB-' to 'BBB'** directly reflects these structural improvements across multiple pillars of its rating framework:

- **Fiscal discipline:** S&P gives heavy weight to the trajectory of fiscal deficits, debt-to-GDP, and debt affordability. Since its scoring system incorporates medium-term government projections, India's glide path from a 9.2% deficit in 2020–21 to 4.4% in 2025–26, along with plans to lower debt-to-GDP by 2030–31, directly strengthens the fiscal score. This is the kind of forward-looking consolidation that S&P recognizes more quickly than Moody's or Fitch.
- **Economic growth:** Even at 6.5% growth, India remains an outlier among large economies. For S&P, nominal GDP growth reduces debt ratios and improves fiscal capacity. Its framework explicitly rewards high growth relative to peers, so this anchors the economic profile positively.
- **Inflation management:** The sharp disinflation to 1.55% in July 2025 improves the monetary assessment, since S&P evaluates whether price stability supports debt sustainability and investor confidence. Unlike Moody's, which looks for consistency across cycles, S&P is quicker to reflect recent credibility gains in inflation and monetary policy in its rating matrix.
- **Combined effect:** Since S&P's rating framework aggregates institutional, economic, fiscal, external, and monetary pillars into a forward-looking matrix, improvements in multiple ratios simultaneously (deficit, debt, growth, inflation) create upward pressure on the indicative rating. With no overriding event risks flagged, the upgrade fits squarely within their published approach.

While S&P has recognized India's recent economic and fiscal improvements with an upgrade, other major rating agencies such as **Moody's and Fitch have not yet adjusted their ratings**. Understanding this divergence requires examining the differences in methodology, emphasis on historical performance versus forward-looking projections, and risk assessment frameworks employed by these agencies. The next section delves into why Moody's and Fitch maintained their existing ratings despite India's strong economic momentum.

3.3. Why Moody's and Fitch did not Upgrade the Rating?

In spite of India's outstanding economic performance, 8.8% average GDP growth, fiscal consolidation from 9.2% to 4.4% deficit, deflation to 1.6%, both Fitch and Moody's have stuck to their current ratings. This departure from the upgrade by S&P is due to differences of approach regarding how these agencies balance near-term improvement with structural weaknesses and depth of institutions.

3.3.1. Moody's Institutional Durability Framework

Moody's retention of its 'Baa3' rating with stable outlook is an indication of the agency's focus on institutional strength over cycle performance. While acknowledging India's strong domestic economic fundamentals, Moody's analytical framework includes what it terms an "event-risk minimum function," where vulnerabilities in any given institutional factor could constrain the overall rating even if others improve.

- **Banking Sector Concerns:** While India's macroeconomic development has been encouraging, Moody's remains skeptical of the structural health of the banking system. Indian banks, especially state-owned banks, still show high ratios of non-performing assets relative to their international counterparts. The agency's judgment does allow for the fact that the vulnerability in the banking system has the potential to quickly convert into fiscal contingent liabilities, given the implicit guarantee of public sector banks by the government. History from emerging markets illustrates how banking crises can quickly undermine otherwise solid fiscal positions—a lesson Moody's includes in its cautious approach.
- **Federal Fiscal Coordination Risks:** While the central government has demonstrated remarkable fiscal discipline, Moody's places considerable stress on the complexities of India's federal arrangement. The state governments' average deficits of 2.7% of GDP reflect fiscal slippage risks that would undermine wider consolidation efforts. The framework developed by the agency suggests risks of fiscal coordination across different levels of government, a challenge that has long plagued federal emerging market economies in periods of political or economic stress.
- **External Vulnerability Test:** Despite India's small net external asset position, Moody's is still cautious about the economy's exposure to external shocks. The approach taken by the agency places considerable weight on India's dependence on crude oil and intermediate goods imports, and on the possibility of "sudden stops" in capital flows which is a phenomenon amply documented in the literature on emerging markets, where sudden reversals in investor sentiment can quickly destabilize otherwise sound fundamentals.
- **Institutional Consistency Requirement:** Moody's belief is that credit stability demands institutional arrangements able to support policy discipline throughout entire economic and political cycles. From this point of view, India's recent progress, though impressive, takes more time to maintain resilience to pass many stress tests before an upgrade can be justified.

3.3.2. Fitch's Structural Debt and Risk Overlay Analysis

Fitch's retention of its 'BBB-' rating reflects the agency's cautious stance in balancing quantitative improvements with persistent structural issues. The agency's Sovereign Rating Model (SRM) reflects India's improved fiscal data; however, its Qualitative Overlay (QO) limits rating upgrades as long as fundamental structural issues are left unresolved.

- **Debt Stock vs. Flow Dynamics:** Fitch acknowledges India's improving fiscal trajectory, but the agency points to the absolute general government debt level at over 80% of GDP, significantly above the BBB category median of about 60%. The agency's methodology distinguishes between improving fiscal flows (deficit control) and reducing the stock of incurred debt to the level of higher-rated comparators. This reflects the wisdom of modern fiscal theory that debt sustainability is not so much about having good current fiscal performance but to arrange debt levels to be adequate buffers against future shocks.
- **Interest Burden Sustainability:** Fitch points to India's interest-to-revenue ratio of 25%, compared with the BBB category median of 8%, reflecting considerably higher debt service burden in relation to fiscal strength. While falling interest rates and robust nominal GDP growth improve debt dynamics, the agency methodology requires tangible evidence that the improved debt service burden would be able to be supported in a range of alternative economic cycles before the improvements are fed into rating calculations.
- **Contingent Liability Universe:** The agency's overlay specifically is mindful of India's extensive public sector enterprise universe and contingent liabilities from financing commitments related to infrastructure. Fitch considers that government balance sheets are wider than accounted-for debt, including implicit guarantees and off-balance-sheet obligations that can crystallize in periods of stress. India's ambitious infrastructure

spending, although growth-supportive, creates potential future fiscal liabilities that the agency includes in its risk assessment.

- **Global Trade Integration Risks:** Fitch's methodology for India accounts for increasing integration into global supply chains as opportunity and risk. Fitch acknowledges that while increasing growth and export competitiveness, integration leaves the economy exposed to global trade tensions and supply chain disruption. Recent geopolitical events, such as the possibility of the United States imposing tariffs on Indian exports, are external risks that would affect both growth expectations and fiscal metrics supporting the current improvement.

3.3.3. Learning from History and Conservative Bias

The restraint exercised by the two agencies is a reflection of lessons learned from past cycles of rating emerging markets, especially in the 1990s and early 2000s. Most economies were then upgraded on the basis of short-term gains but then later downgraded as structural problems re-emerged.

- **Asian Financial Crisis Precondition:** The 1997-98 Asian Financial Crisis demonstrated how economies with strong growth and budgetary health could rapidly degenerate with the tightening of external financing conditions. Economies like Thailand and South Korea, which had benefited from positive ratings based on strong economic performance, experienced steep downgrades when structural vulnerabilities like banking system weaknesses and external dependence became apparent under crisis conditions.
- **Institutional Memory Effect:** Moody's and Fitch have an institutional memory regarding ratings volatility encountered during previous periods of stress in emerging markets. This shared experience underlies their tendency to require steady evidence of structural improvement rather than extrapolating from short-term trends. The agencies' conservatism is a professional commitment to rating stability and credibility over sensitivity to short-run improvements.
- **Post-2008 Recalibration:** The 2008 financial crisis made clear the pace at which sovereign credit conditions can deteriorate, even in advanced economies, prompting a widespread recalibration towards more conservative rating habits. This experience has had a specific impact on the way agencies evaluate debt levels and contingent liabilities, in which India is still lagging, with recent improvements.

The methodological divergence thus represents complementary rather than contradictory analytical perspectives. S&P's upgrade validates India's policy momentum and implementation credibility, while Moody's and Fitch's patience reflect the deeper institutional transformations required for comprehensive rating recognition. For India, this suggests that continued policy implementation, institutional strengthening, and demonstrated resilience through economic cycles will be necessary to achieve consensus upgrade recognition across all major rating agencies.

Chapter 4: Macro and policy implications

S&P's upgrade of India's sovereign rating from 'BBB-' to 'BBB' represents more than a technical adjustment, it signals a fundamental shift in how international markets perceive India's creditworthiness and economic trajectory. This chapter examines the immediate macroeconomic implications of the upgrade, analyzes historical precedents where rating changes influenced policy directions, and evaluates how the upgrade affects India's fiscal targets and budget framework.

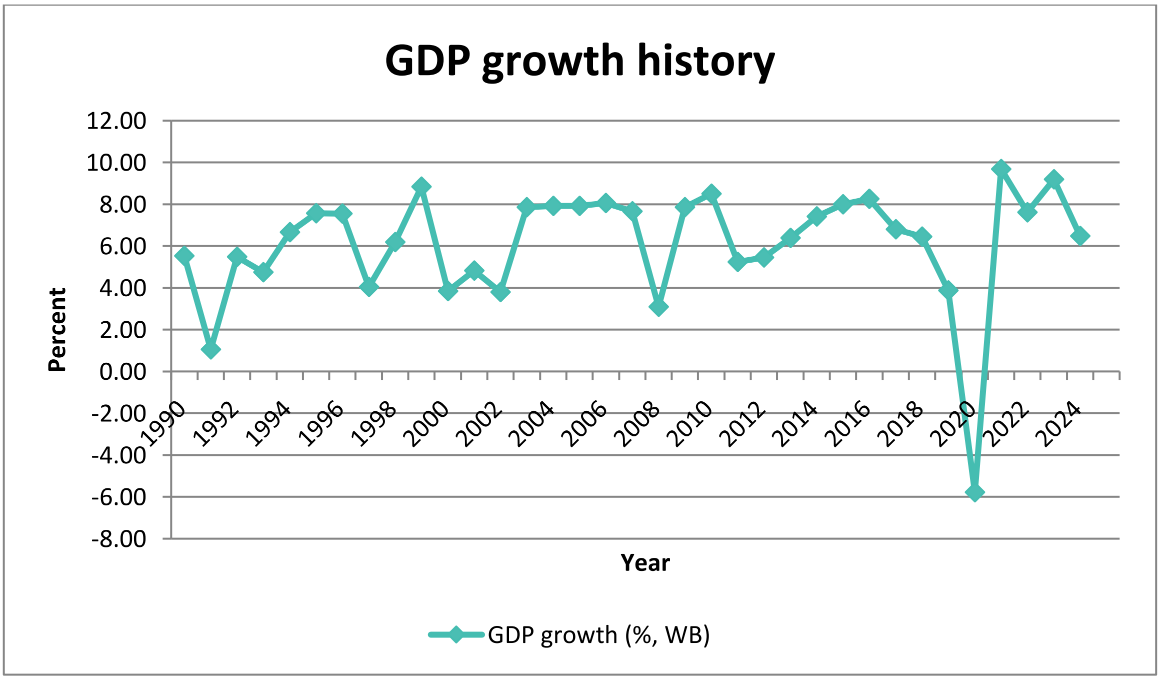
4.1. Immediate Macroeconomic Impact

S&P's upgrade of India from *BBB-* to *BBB* in August 2025 is significant for both symbolic and material reasons. Sovereign ratings are a key determinant of country risk premiums, external borrowing costs, and the cost of capital for both government and private sector entities.

In the immediate term, the upgrade lowers India's **sovereign spread** and reduces borrowing costs:

- **GDP Growth:** India's GDP growth rebounded sharply after the 2020 contraction (–6.6%), stabilizing in the 6–8% range during 2022–24. This resilience in growth was a key determinant in S&P's decision, as sustained high growth improves debt-servicing capacity.

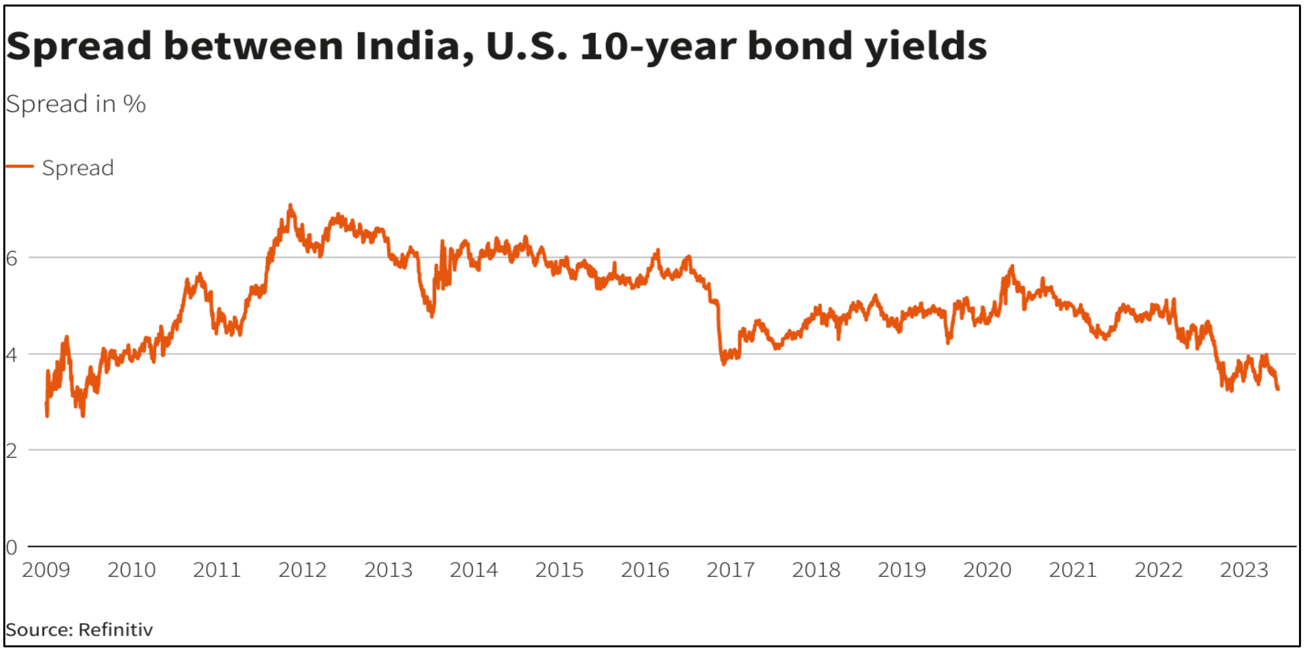
Figure 1: India's GDP Growth History



India's cyclical growth, highlighting recoveries during upgrade phases (2004–07, 2017, 2025) (source).

- **Bond Yields: Bond Yields:** Historically, rating upgrades have been followed by modest reductions in India's 10-year G-Sec yields. For instance, after S&P's upgrade on 14 August 2025, the benchmark yield fell by **7–10 basis points** during the day which was the sharpest single-day decline in two months (Business Standard, Reuters, Financial Express). Given the government's gross borrowing program of ₹14–15 trillion, even a 10-bps reduction translates into savings of around ₹140–150 billion in annual interest payments (approximately 0.05% of GDP).

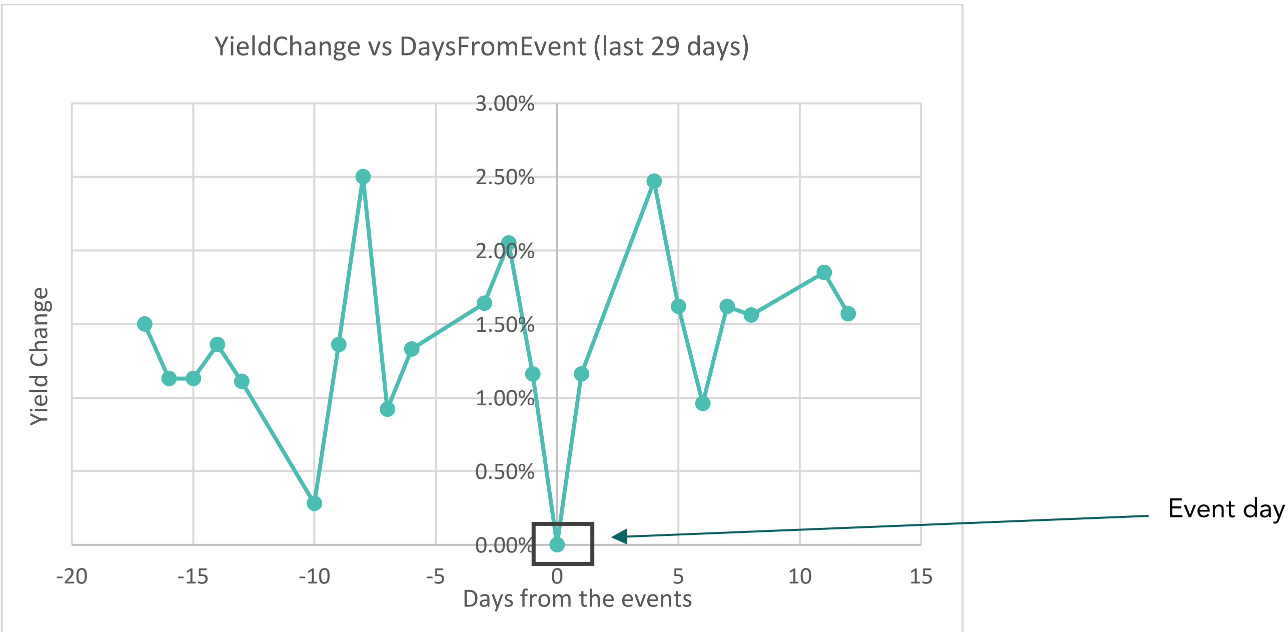
Figure 2: India's 10-year G-Sec yield vs EMBI spreads, with 2007, 2017, and 2025 upgrades marked



This demonstrates how ratings compress sovereign spreads and borrowing costs.

Beyond tracking broad trends, bond yields also offer a useful lens to test whether rating announcements themselves alter investor behavior.

Figure 3: Showing last 29 days' yield change

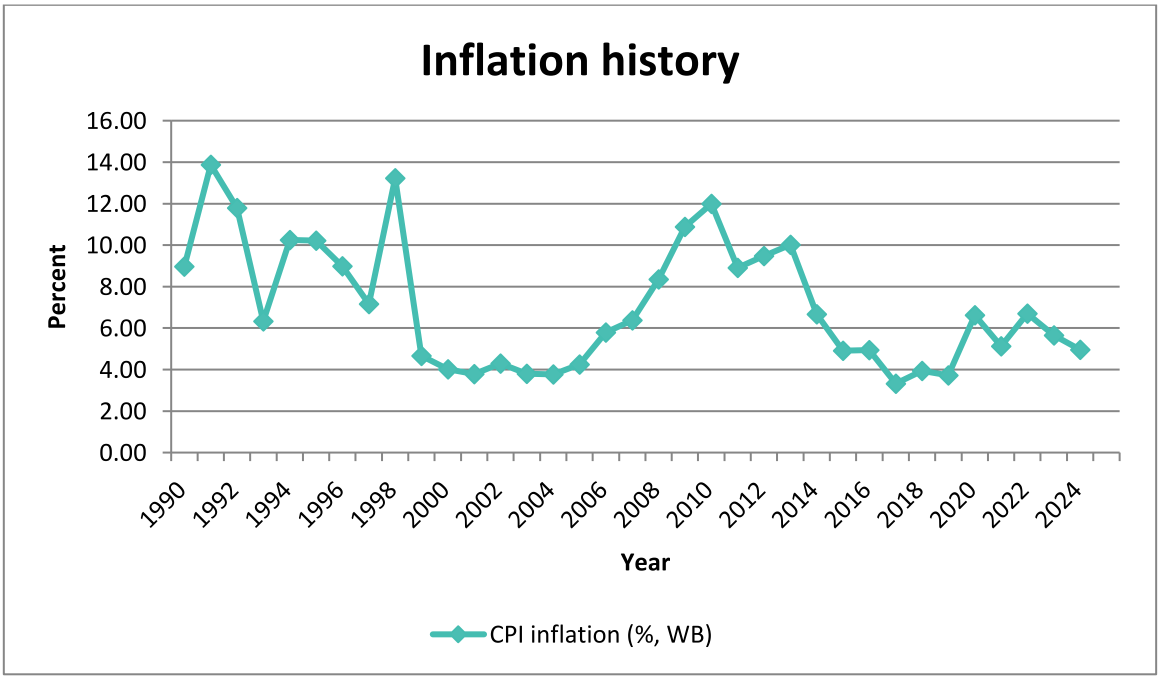


Source

Bond yields are not only a reflection of domestic macroeconomic conditions but also a real-time barometer of how investors perceive creditworthiness. To assess whether rating actions carry informational value for the market, we employ an event study around sovereign rating announcement. The logic is straightforward: if investors view an upgrade as credible and material, the 10-year G-Sec yield should compress as the risk premium declines; if a downgrade occurs, yields should widen to reflect heightened risk. By examining movements in yields in narrow windows before and after rating changes, we can distinguish between shifts driven by the rating action itself and those attributable to broader global or domestic factors.

- **Capital Flows:** Past upgrades (2007, 2017) triggered foreign portfolio inflows of 0.2–0.4% of GDP within 12 months. With India's GDP at ~$4.1 trillion, similar flows could bring ~$8–12 billion in 2025–26, strengthening FX reserves and stabilizing the rupee.
- **Currency & Inflation:** The upgrade narrows the sovereign risk premium, improving rupee stability. Since India imports ~$120 billion in crude annually, even a 1% appreciation of INR/USD reduces the oil import bill by over $1 billion, easing imported inflation pressures.

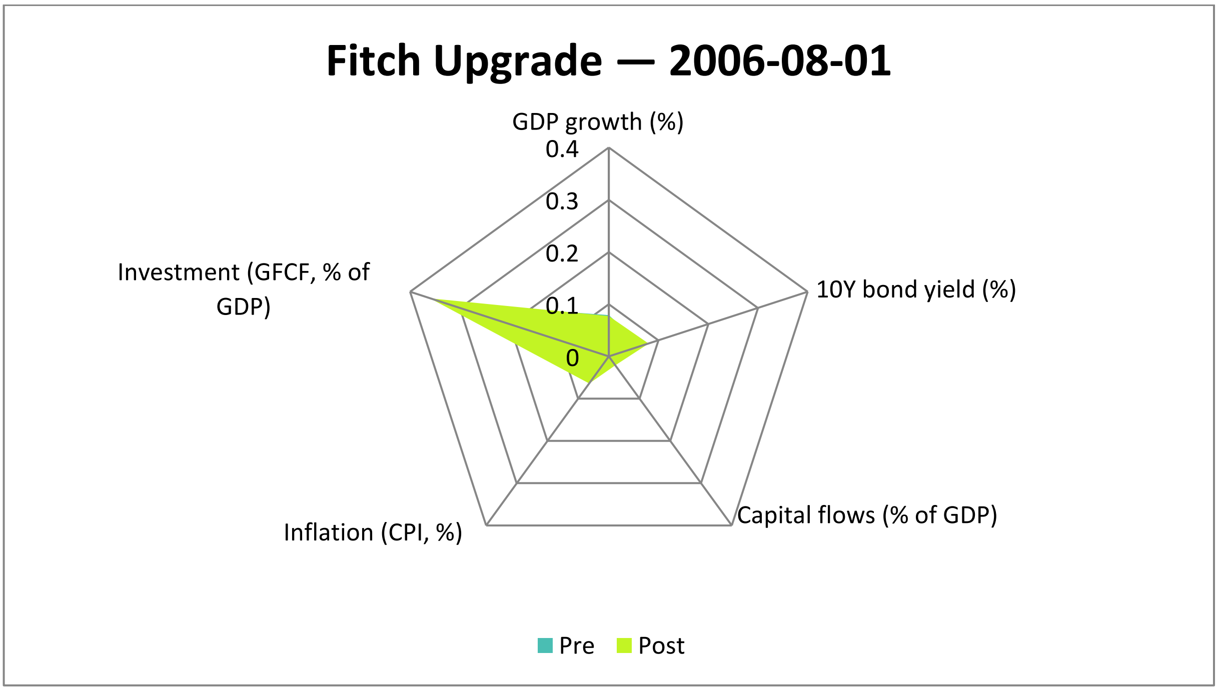
Figure 4: India's CPI inflation history (1990–2024)

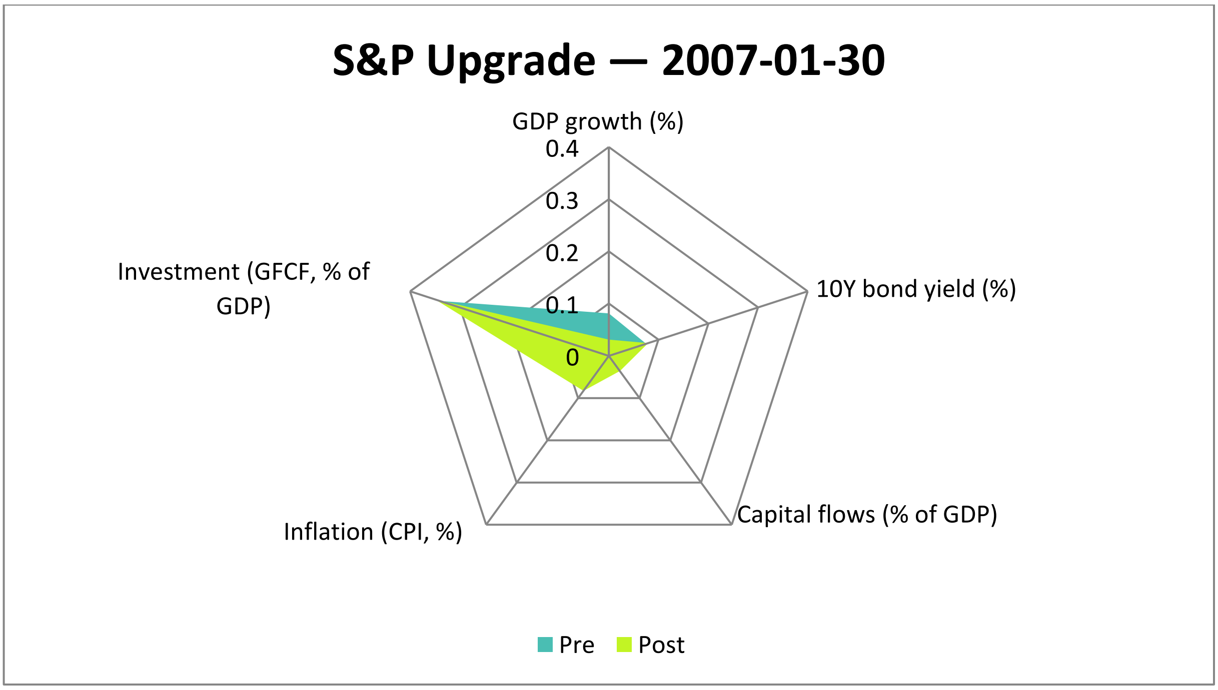


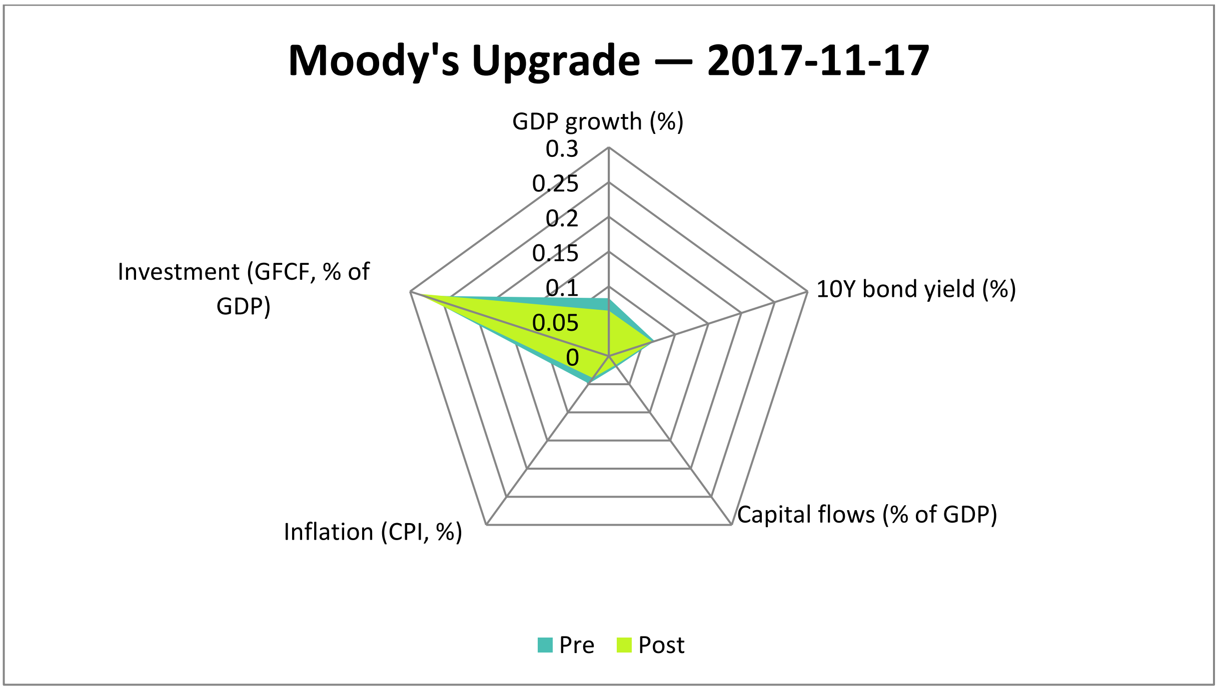
Shows inflation spikes in 2011–13 and moderation to ~5% in 2024, supporting the upgrade. (source)

- **Investment flows:** Empirical literature and past episodes show heterogeneous investor responses to sovereign upgrades. Pension funds and large institutional investors typically view upgrades as positive for long-term allocation but often make only incremental portfolio changes due to liability matching constraints. Mutual funds and other portfolio managers are more responsive, especially funds benchmarked to EM bond indices where upgrades can trigger index re-weighting or attract new index-tracking inflows. Historical episodes (India 2007, 2017) show modest but measurable portfolio inflows (0.2–0.4% of GDP within 12 months) after upgrades; banks and other FIs benefited via lower funding costs and some compression in corporate spreads. For FDI, the link is weaker and longer-lived, upgrades can improve sentiment and ease financing for cross-border acquisitions, but FDI decisions depend more on structural competitiveness than short-term rating changes. (SSRN, cemla.org)

Figure 5: Impact of Rating upgrade on KPIs







(Source: World bank, Trading Economics, RBI Handbook of Statistics)

Fitch upgrade (2006): The radar compares 2005 (pre) and 2007 (post). After the Fitch upgrade, capital flows and investment rose (0.9% -> 2.1% of GDP, 33% -> 36%), consistent with improved sovereign perception that attracted financing and supported capex. However, inflation rose sharply (4.2% -> 6.4%), and nominal 10-year yields increased (6.7% -> 8.0%), indicating that inflationary pressures and broader market conditions dominated yields despite the upgrade. GDP remained broadly stable (7.9% -> 7.7%). The pattern is consistent with an upgrade that boosts flows/investment while concurrent macro drivers push inflation and yields higher.

S&P upgrade (2007): Pre/post comparison uses 2006 -> 2008. The post year (2008) shows a sharp GDP slowdown (8.1% → 3.1%) and higher inflation (5.8% -> 8.3%), reflecting that the post window captures the global dislocation culminating in late 2008. Capital flows and investment rose on average across the window, likely reflecting strong inflows in 2007 (post-upgrade) before the reversal but the large GDP decline means this calendar-year pair mixes upgrade effects with a major exogenous shock.

Moody's upgrade (2017): Comparing 2016 -> 2018, inflation and yields eased (inflation 4.9% -> 3.9%; 10Y yields 6.90% → 6.58%) and investment rose slightly (28% -> 29%). That is a pattern consistent with an upgrade improving funding conditions and inflation dynamics, even as growth moderated (8.3% -> 6.5%) due to contemporaneous cyclical and policy factors.

Rating upgrades improve sovereign credibility and reduce the sovereign risk premium, which, through portfolio reallocation and lower corporate funding costs, tends to boost capital inflows and investment. However, nominal sovereign yields are a compound outcome: they reflect not only the sovereign risk premium but also expected inflation, the monetary policy response, and supply/term-premium effects. Consequently, an upgrade may coincide with falling yields (when inflation and term premium ease, as in Moody's 2017) or with rising yields if inflation or issuance pressures dominate (as in the 2006–08 window). In open economies, global shocks (commodity spikes, global financial stress) can swamp upgrade effects and produce seemingly paradoxical combinations (more inflows but lower growth and higher inflation), so interpretation must always account for contemporaneous macro-financial forces

The immediate macroeconomic impact of the rating upgrade thus creates a foundation for the broader policy implications discussed in the following sections. The quantified benefits across these five parameters demonstrate how sovereign creditworthiness improvements translate into concrete economic advantages, while the enhanced policy credibility provides the institutional framework necessary for sustaining these gains over the medium term.

4.2. Historical Rating and Policy Linkages

Sovereign rating changes have historically catalyzed policy adjustments and institutional reforms, as governments seek to either capitalize on positive momentum or address vulnerabilities highlighted by rating agencies. India's experience, along with international precedents, demonstrates how rating actions can influence policy priorities and reform trajectories.

India’s sovereign rating history illustrates a cyclical relationship between macroeconomic stability, policy reforms, and agency actions.

- **2004–07 Upgrade Cycle:** The enactment of the FRBM Act (2003), fiscal consolidation, and >8% GDP growth drove successive upgrades. By 2007, S&P rated India investment grade (*BBB-*), coinciding with strong macro fundamentals (debt-to-GDP ~66%, fiscal deficit ~3.3%).

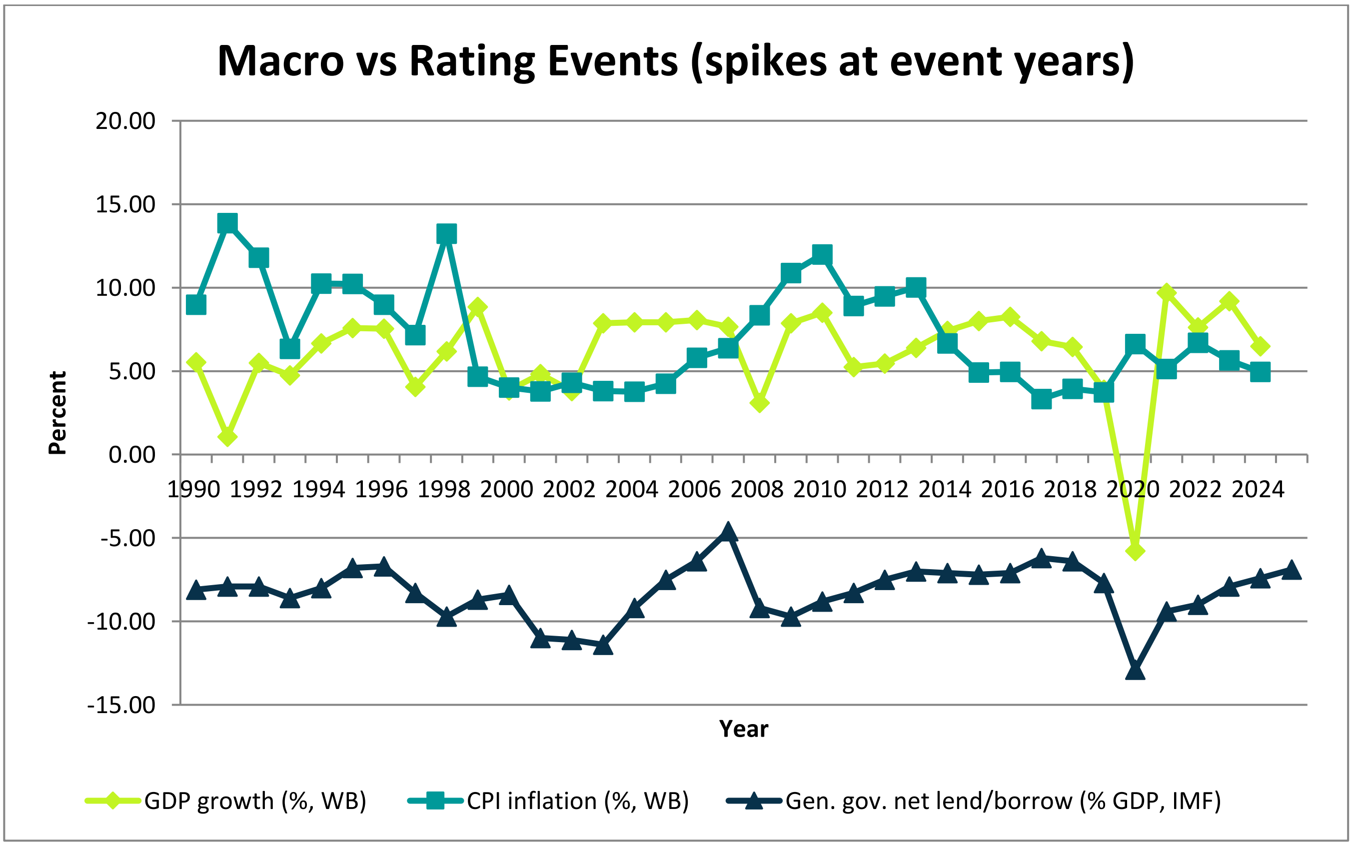
- **2011–13 Negative Cycle:** High CPI inflation (>10%), twin deficits (CAD >4% of GDP, fiscal >5.5%), and slowing growth (~5%) led to negative outlooks from all agencies. Policy responses included deregulation of fuel prices and fiscal tightening.

- **2017 Upgrade (Moody’s):** The GST rollout, IBC implementation, and formal inflation targeting restored credibility. Moody’s upgraded India to *Baa2*. Yields fell 40 bps in the subsequent quarter, supporting corporate borrowing and investment.

- **2020 Pandemic Shock:** GDP contracted by –6.6% in FY21; the fiscal deficit ballooned to 9.2%. Moody’s downgraded to *Baa3*, while S&P and Fitch retained *BBB-* but with a negative outlook. Policy responses were targeted fiscal support and RBI’s liquidity measures.

- **2025 Upgrade (S&P):** With GDP growth stabilizing at 6.5–7%, CPI moderating to ~5%, and the fiscal deficit narrowing to 5.1% in FY25, S&P recognized India’s reform trajectory and debt sustainability path, moving the sovereign to *BBB*.

Figure 6: Macro indicators vs rating events (1990–2025)



This graph shows spikes at rating years, reinforcing the cyclical link.

4.3. Peer Comparison

Cross-country experiences over the past decade illustrate that sovereign rating changes are rarely isolated technical adjustments; they reflect broader narratives of credibility, policy discipline, and resilience. To contextualize India's recent upgrade, it is useful to examine how peer economies such as Mexico, Indonesia, Greece, Brazil, South Africa, and Turkey have experienced rating revisions during 2015–2025. These examples reveal the interplay between fiscal performance, institutional strength, and external vulnerabilities in shaping agency actions and market outcomes.

Table 3: Peer Comparison on how other countries were impacted due to the rating change

COUNTRY	MAJOR RATING MOVES (2015–2025)	PRIMARY REASONS AGENCIES GAVE	OBSERVED MARKET / POLICY AFTERMATH
MEXICO	Moody's cut Mexico one notch to Baa2 (Aug/Jul 2022) and later shifted outlooks (2024–2025: outlook changes/concerns). S&P/Fitch actions since 2022–25 mostly affirmations with watch/outlook moves. (Reuters)	Moody's: weakening policy framework, weaker investment prospects, increased structural rigidities and fiscal pressures; later Moody's flagged institutional/policy risks (rule-of-law, fiscal slippage). (Reuters)	Markets: rating action prompted reassessment of Mexican sovereign & bank credits; some increase in risk premia and downgrade spillovers to state-owned firms (e.g., PEMEX). Policy: government rhetoric and fiscal signals adjusted; central bank and markets priced in higher political/institutional risk. (finanzaspublicas.hacienda.gob.mx, Reuters)
INDONESIA	Largely stable investment-grade ratings across major agencies through 2015–2025 (e.g., Fitch affirmed BBB / Mar 2025; Moody's Baa2 stable). No major multi-notch	Agencies cite resilient growth, prudent debt ratios, comfortable external buffers, and credible macro management; occasional concerns over political risks	Aftermath: stable access to international markets, modest compression in CDS/spreads when macro prints improved; lower volatility in yields relative to peers. The stability supported steady capital inflows and infrastructure financing. (Fitch Ratings)

	downgrades in the decade. (Fitch Ratings, Trading Economics)	and commodity exposure but not enough to change grade. (Fitch Ratings, Trading Economics)	
GREECE	From junk -> back to investment grade in the 2018–2024 window (series of upgrades culminating recently — credit improvement visible 2023–2025). Several agencies upgraded as debt ratios fell and banks healed. (Reuters, Bank of Greece)	Main drivers: large reduction in debt/GDP trajectory, stronger primary balances, stabilisation and recapitalisation of banks, EU support / favourable Eurozone conditions. Agencies emphasised improved fiscal performance and lower contingent liabilities. (Reuters, Scope Ratings)	Aftermath: sharply narrower spreads vs core Europe, lower borrowing costs for government and banks, improved investor confidence and re-entry of foreign investors — aided tourism recovery and GDP convergence. Central bank / EU support also made upgrades more credible. (See Bank of Greece empirical estimates of positive real effects from upgrades.) (Reuters, Bank of Greece)
BRAZIL	Major downgrades 2015–2016 (S&P/Fitch/Moody's moved Brazil toward or into junk in that period); post-2016 gradual stabilisation but rating stayed under pressure through political & fiscal cycles. (Reuters)	Fiscal deterioration, political crisis, recession (2015–16), weak medium-term fiscal reforms initially; agencies pointed to rising debt, fiscal slippage and political risks. (Reuters)	Aftermath: immediate bond sell-offs and higher yields, forced-selling concerns for funds indexed to investment-grade, higher borrowing costs for sovereign & corporates; led to stronger emphasis by policymakers on fiscal adjustment and reforms in some periods. Market volatility persisted around political events. (Reuters)
SOUTH AFRICA	2017: S&P and Fitch moves pushed South Africa into or near sub-investment grade territory (2016–2017). Gradual signals of improvement later but rating not fully restored to pre-2015 levels. (ResearchGate, Moonstone)	Agencies cited governance deterioration, fiscal-balance deterioration, rising public debt, and political instability (including events affecting the state-owned enterprises). (ResearchGate, Scope Ratings)	Aftermath: sharp one-day spikes in 10-yr yields and wider spreads when downgrades/outlooks changed (empirical studies document multi-basis-point jumps), capital outflows and weaker rand; fiscal tightening and governance reforms discussed as corrective policy responses. (ResearchGate, Moonstone)
TURKEY	Multiple downgrades across the decade (notably around 2018 currency crisis and later as inflation surged); ratings fell due to external vulnerabilities, policy-making concerns and high inflation. (ResearchGate, ScienceDirect)	Agencies pointed to weak central-bank independence, unorthodox macro policy, high inflation, sharp lira depreciation and rising external financing risks. Political interference and rapid FX moves were repeatedly flagged. (ResearchGate, ScienceDirect)	Aftermath: dramatic FX depreciation episodes, spikes in sovereign spreads and borrowing costs, foreign investor pullback at times; domestic monetary/fiscal responses (tightening or unconventional measures) followed, but credibility problems persisted and raised long-term risk premia. (ResearchGate, ScienceDirect)

Table 3 summarizes major rating movements for six large emerging or recently stressed economies. Each entry highlights the rating agencies' stated rationale and the observed aftermath in financial markets and policy responses. The comparison shows a spectrum of experiences: stable performers like Indonesia that maintained investment-grade status through consistent macroeconomic management; reform-driven comebacks such as Greece, where debt reduction and EU support enabled an upgrade back to investment grade; and cautionary cases like Brazil, South Africa, and Turkey, where political instability, fiscal slippage, or policy credibility concerns triggered downgrades with significant spillovers to borrowing costs and investor confidence. By juxtaposing these cases, the table provides a benchmark to interpret India's trajectory within a broader global frame.

The evidence from peers underscores two key lessons. First, rating upgrades are neither permanent nor guaranteed; they require continuous reinforcement through fiscal consolidation, institutional credibility, and resilience against external shocks. Second, downgrades often come swiftly when vulnerabilities outweigh growth momentum, amplifying financing costs and constraining policy space. Against this backdrop, India's recent upgrade by S&P can be seen both as recognition of strong fundamentals and as a reminder that sustaining credibility demands consistency across cycles—an insight reinforced by the diverse experiences of its peers over the past decade.

4.4. Impact on India's Budget Targets and Fiscal Framework

The rating upgrade creates both opportunities and challenges for India's fiscal framework, influencing borrowing costs, policy flexibility, and the credibility of medium-term fiscal targets. Understanding these effects is crucial for evaluating how the upgrade might shape future budget strategies and policy priorities.

4.4.1. Debt Sustainability and Fiscal Space Enhancement

Improved Debt Dynamics: The rating upgrade enhances India's debt sustainability metrics through multiple channels. Lower borrowing costs reduce interest payments as a share of revenues, creating fiscal space for development spending or faster deficit reduction. Even a modest 25-50 basis point reduction in average borrowing costs translates to savings of 0.1-0.2% of GDP annually, given India's debt stock of approximately 85% of GDP.

Medium-Term Fiscal Target Credibility: The upgrade strengthens the credibility of India's medium-term fiscal consolidation path, including the target to reduce the central government deficit to 4.4% of GDP by 2025-26 and the broader goal of reducing general government debt to around 60% of GDP by 2030-31. Enhanced credibility makes these targets more achievable by reducing market skepticism and political pressure for fiscal expansion.

Contingent Liability Management: Improved sovereign creditworthiness provides additional headroom for managing contingent liabilities, including potential support for public sector enterprises, state governments, or financial institutions during stress periods. This enhanced fiscal flexibility is particularly valuable given India's large public sector and development finance requirements.

4.4.2. Infrastructure Investment and Capital Expenditure Implications

Enhanced Infrastructure Financing Capacity: The rating upgrade supports India's ambitious infrastructure investment targets by reducing financing costs and improving access to long-term capital. The government's plan to invest 5.5% of GDP in infrastructure becomes more financially sustainable when funding costs decline and international financing options expand.

Public-Private Partnership Viability: Lower sovereign risk premiums improve the viability of public-private partnerships by reducing the cost of capital for private partners and enhancing government payment credibility. This is particularly important for India's infrastructure development strategy, which relies heavily on private sector participation and long-term contractual arrangements.

State Government Fiscal Coordination: The upgrade indirectly benefits state governments through improved market access and lower borrowing costs, given their linkage to sovereign creditworthiness. This enhanced state-level fiscal capacity supports national infrastructure and development objectives while maintaining overall fiscal discipline.

4.4.3. Monetary-Fiscal Policy Coordination Enhancement

Central Bank Policy Flexibility: The rating upgrade provides additional support for Reserve Bank of India monetary policy by reducing external financing risks and enhancing policy credibility. This flexibility is particularly valuable as India navigates global monetary policy transitions and manages domestic inflation dynamics.

External Sector Policy Integration: Improved sovereign creditworthiness enhances the effectiveness of external sector policies, including capital account management and foreign exchange intervention strategies. The upgrade reduces the risk of sudden capital flow reversals and provides additional policy space for managing external volatility.

Development Finance Integration: The upgrade supports India's development finance strategy by improving the creditworthiness of development finance institutions and enabling more efficient capital allocation toward priority sectors including renewable energy, manufacturing, and digital infrastructure.

4.4.4. Budget Strategy and Policy Prioritization

Revenue Enhancement Opportunities: The upgrade creates conditions for improved tax compliance and revenue mobilization by enhancing economic growth prospects and business confidence. Higher growth and improved business sentiment typically translate to better tax collection efficiency and voluntary compliance.

Expenditure Quality Focus: With improved financing conditions, budget strategy can shift toward expenditure quality enhancement rather than pure fiscal consolidation. This includes increased emphasis on productivity-enhancing investments, social infrastructure development, and institutional capacity building.

Reform Sequencing Advantages: The rating upgrade provides political capital and market confidence for implementing potentially disruptive but necessary reforms, including labor market flexibility enhancement, land acquisition streamlining, and further financial sector strengthening. The improved external environment creates space for domestic reform implementation.

Crisis Preparedness Enhancement: Improved sovereign creditworthiness provides additional fiscal space for responding to future economic shocks, whether domestic or external in origin. This enhanced resilience is particularly valuable given global economic uncertainties and the need for flexible policy responses to unexpected developments.

The rating upgrade thus creates a virtuous cycle where improved creditworthiness enhances policy effectiveness, which in turn supports further improvements in fundamentals and institutional capacity. For India's budget framework, this translates to enhanced fiscal sustainability, improved policy flexibility, and stronger foundations for achieving ambitious development objectives while maintaining macroeconomic stability.

4.5. Impact of Downgrade of a Rating:

While S&P's recent upgrade of India's sovereign rating represents a positive milestone, understanding the potential consequences of rating deterioration provides critical context for policymakers and market participants. Sovereign rating downgrades can trigger cascading effects that extend far beyond government borrowing costs, creating self-reinforcing cycles of capital flight, currency weakness, and economic stress. Historical precedents from emerging markets demonstrate how quickly confidence can erode when structural vulnerabilities are exposed, transforming manageable fiscal imbalances into systemic crises. For India, analyzing these downside risks is essential not only for crisis preparedness but also for understanding the policy discipline required to maintain and build upon recent rating improvements.

- Fiscal Deterioration: A sharp increase in fiscal deficits beyond the projected 4.4% of GDP target, or failure to implement the debt-to-GDP reduction path to 60% by 2030-31. Rating agencies particularly monitor debt sustainability metrics and interest-to-revenue ratios (currently at 25% for India, compared to BBB median of 8%).
- Banking System Crisis: Given Moody's specific concerns about India's banking sector health, a major banking crisis requiring government bailouts could rapidly crystallize contingent liabilities. The implicit guarantee on public sector banks creates direct fiscal exposure.
- External Sector Stress: Despite India's modest net external asset position, sudden capital flow reversals or a sharp deterioration in the current account deficit (particularly if oil prices spike) could trigger downgrades. India's dependence on crude oil imports creates vulnerability to external shocks.
- Inflation Resurgence: A return to the high inflation environment of 2011-13 (>10% CPI) would undermine monetary credibility and debt sustainability, particularly given India's recent disinflation success.
- Political/Policy Discontinuity: Major policy reversals, weakening of institutional frameworks like inflation targeting, or significant political instability affecting reform implementation.

The analysis of downgrade risks underscores the fragility that underlies even improved sovereign ratings. Historical precedents demonstrate that rating deterioration creates self-reinforcing negative cycles where capital flight exacerbates the fundamental weaknesses that initially triggered agency concerns. For India, the lesson is clear:

maintaining the policy discipline that earned the recent S&P upgrade requires continuous attention to fiscal sustainability, institutional strength, and structural reform implementation. The asymmetric nature of rating changes where downgrades often occur more rapidly and with greater market impact than upgrades, emphasizes that preserving creditworthiness is ultimately more challenging than achieving it. As India continues its development trajectory, understanding these downside risks provides essential context for policy formulation and helps explain why rating agencies like Moody's and Fitch maintain their cautious approach despite acknowledging the country's recent improvement.

Chapter 5: Conclusion

The upgrade in India's sovereign rating is a moment worth noting but it should not be mistaken for the final destination. At its core, the change signals confidence in India's growth momentum, fiscal discipline, and inflation control. Yet, the fact that not all rating agencies moved in the same direction shows that doubts remain about the depth and durability of these improvements.

This divergence tells us something important: ratings are not only about numbers on debt or growth. They reflect how much trust the world has in a country's ability to sustain reforms, to manage crises, and to follow through on its commitments across political and economic cycles. India's current story is one of strong recovery and resilience, but also of unfinished work whether in strengthening its banking system, improving coordination between the central and state governments, or reducing heavy debt burdens.

My own view is that ratings should be treated as checkpoints, not victories. They validate progress but also highlight where gaps remain. For India, the challenge is to ensure that reforms are not just headline measures but deeply rooted in institutions and governance. Short-term growth can earn applause, but only long-term credibility earns trust. The risk of relying too much on momentum is that external shocks or policy reversals can undo hard-won gains very quickly.

At the same time, this upgrade can serve as useful leverage. It lowers borrowing costs, attracts investors, and builds confidence but only if this moment is used wisely. If India can channel this confidence into deeper reforms, better fiscal management, and inclusive development, then future upgrades will not just be acknowledgements of growth spurts, but recognition of a system built to last.

In that sense, the recent rating change is both a reward and a warning. It rewards the progress made so far, but it warns that credibility in global markets has to be earned again and again. India's real task is to make sure that its story is not only about momentum, but about building an economy that can stand steady through every cycle, with or without the approval of rating agencies.

Annexure

Table 4: India's Credit Rating History

Agency	Rating	Outlook	Date
Standard & Poor's	BBB	Stable	8/2025
Fitch	BBB-	Stable	8/2024
Standard & Poor's	BBB-	Positive	5/2024
Fitch	BBB-	Stable	1/2024
Moody's	Baa3	Stable	8/2023
Fitch	BBB-	Stable	5/2023
Fitch	BBB-	Stable	12/2022
Fitch	BBB-	Stable	6/2022
Fitch	BBB-	Negative	11/2021
Moody's	Baa3	Stable	10/2021
Fitch	BBB-	Negative	4/2021
Moody's	Baa3	Negative	6/2020
Fitch	BBB-	Negative	6/2020
Fitch	BBB-	Stable	12/2019
Moody's	Baa2	Negative	11/2019
Fitch	BBB-	Stable	4/2019
Fitch	BBB-	Stable	4/2018
Moody's	Baa2	Stable	11/2017
Fitch	BBB-	Stable	5/2017
Moody's	Baa3	Positive	11/2016
Fitch	BBB-	Stable	7/2016
Fitch	BBB-	Stable	12/2015
Moody's	Baa3	Positive	4/2015

Standard & Poor's	BBB-	Stable	9/2014
Fitch	BBB-	Stable	8/2014
Fitch	BBB-	Stable	6/2014
Fitch	BBB-	Stable	5/2014
Fitch	BBB-	Stable	4/2014
Fitch	BBB-	Stable	3/2014
Fitch	BBB-	Stable	1/2014
Fitch	BBB-	Stable	12/2013
Fitch	BBB-	Stable	8/2013
Fitch	BBB-	Stable	6/2013
Fitch	BBB-	Negative	10/2012
Fitch	BBB-	Negative	7/2012
Standard & Poor's	BBB-	Negative	4/2012
Moody's	Baa3	Stable	12/2011
Fitch	BBB-	Stable	12/2011
Fitch	BBB-	Stable	6/2011
Fitch	BBB-	Stable	6/2010
Standard & Poor's	BBB-	Stable	3/2010
Moody's	Baa3	Stable	12/2009
Standard & Poor's	BBB-	Negative	2/2009
Fitch	BBB-	Stable	7/2008
Standard & Poor's	BBB-	Stable	1/2007
Fitch	BBB-	Stable	8/2006
Moody's	Baa3	Stable	5/2006
Standard & Poor's	BB+	Positive	4/2006
Standard & Poor's	BB+	Stable	11/2005
Standard & Poor's	BB+	Stable	11/2005

Standard & Poor's	BB+	Stable	2/2005
Standard & Poor's	BB	Positive	8/2004
Moody's	Baa3	Stable	1/2004
Fitch	BB+	Stable	1/2004
Standard & Poor's	BB	Stable	12/2003
Moody's	Ba1	Under Review	11/2003
Standard & Poor's	BB	Negative	9/2002
Fitch	BB	Stable	11/2001
Standard & Poor's	BB	Negative	8/2001
Fitch	BB+	Negative	5/2001
Standard & Poor's	BB	Stable	10/2000
Fitch	BB+	Stable	9/2000
Standard & Poor's	BB	Positive	3/2000
Standard & Poor's	BB	Stable	10/1998
Standard & Poor's	BB+	Negative	5/1998
Standard & Poor's	BB+	Stable	10/1997
Standard & Poor's	BB+	Positive	10/1996
Standard & Poor's	BB+	Stable	9/1991
Standard & Poor's	BBB-	Negative watch	3/1991
Standard & Poor's	BBB	Stable	9/1990

Table 5: Hierarchy of the Ratings

S&P	Fitch	Moody's	Grade
AAA	AAA	Aaa	Investment grade: Prime
AA+	AA+	Aa1	High Grade
AA	AA	Aa2	
AA-	AA-	Aa3	
A+	A+	A1	Upper Medium Grade
A	A	A2	
A-	A-	A3	

BBB+	BBB+	Baa1	Lower Medium Grade
BBB (India)*	BBB	Baa2	
BBB-	BBB- (India)*	Baa3 (India)*	
BB+	BB+	Ba1	Non-Investment Grade: Speculative
BB	BB	Ba2	
BB-	BB-	Ba3	
B+	B+	B1	Highly Speculative
B	B	B2	
B-	B-	B3	
CCC+	CCC+	Caa1	Substantial Risk
CCC	CCC	Caa2	
CCC-	CCC-	Caa3	
CC	CC	Ca	Extremely speculative
C	C	C	