

Stewart & Mackertich Research had issued a note on “The biggest surprise may be, around the corner - A ratings upgrade on India” dated October 26, 2017 and updated one on November 01, 2017, reasoning several points on India's rating upgradation. Within less than a month, Moody's Investors Service upgraded India's sovereign ratings.

Please find the link of our earlier report below:

<http://www.smifs.com/UploadResearch/Update%20on%20-%20A%20rating%20upgrade%20on%20India%20is%20likely.pdf1.pdf>

Moody's Investors Service has upgraded India's sovereign ratings to "Baa2" from "Baa3" and changed the outlook on the rating to "stable" from "positive".

International rating agency Moody's Investors Service upgraded India's sovereign ratings to "Baa2" from its lowest investment grade "Baa3" and changed the outlook for India's rating to "stable" from "positive". Moody's also raised India's long-term foreign-currency bond ceiling to "Baa1" from "Baa2", and the long-term foreign-currency bank deposit ceiling to "Baa2" from "Baa3". The short-term foreign-currency bond ceiling remains unchanged at "P-2", and the short-term foreign-currency bank deposit ceiling has been raised to "P-2" from "P-3". The long-term local currency deposit and bond ceilings remain unchanged at "A1". It has also upgraded India's local currency senior unsecured rating to "Baa2" from "Baa3" and its short-term local currency rating to "P-2" from "P-3".

According to a statement from the agency, the decision to upgrade the ratings is underpinned by Moody's expectation that continued progress on economic and institutional reforms will, over time, enhance India's high growth potential and its large and stable financing base for Government debt, and will likely contribute to a gradual decline in the general Government debt burden over the medium term. However, India's high debt burden remains a constraint on the country's credit profile, Moody's believes that the reforms put in place have reduced the risk of a sharp increase in debt, even in potential downside scenarios.

According to Moody's, India's growth potential is significantly higher than most other "Baa"-rated sovereigns.

While a number of important reforms remain at the design phase, Moody's believes that those implemented to date will advance the Government's objective of improving the business climate, enhancing productivity, stimulating foreign and domestic investment, and ultimately fostering strong and sustainable growth. The reform program will thus complement the existing shock-absorbance capacity provided by India's strong growth potential and improving global competitiveness. Among other things, it acknowledged improvements to the monetary policy framework; measures to address the overhang of non-performing loans (NPLs) in the banking system, and measures such as demonetisation, the Aadhaar system of biometric accounts and targeted delivery of benefits through the Direct Benefit Transfer (DBT) system intended to reduce informality in the economy. "Other important measures which have yet to reach fruition include planned land and labor market reforms, which rely to a great extent on cooperation with and between the States," it said.

However, the rating agency maintained that most of these measures will take time for their impact to be seen, and some, such as the GST and demonetisation, have undermined growth over the near term. Moody's expects real GDP growth to moderate to 6.7% in the fiscal year ending in March 2018. "However, as disruption fades, assisted by recent government measures to support SMEs and exporters with GST compliance, real GDP growth will rise to 7.5% in FY2018 (2018-19), with similarly robust levels of growth from FY2019 (2019-20) onward. Longer term, India's growth potential is significantly higher than most other "Baa"-rated sovereigns," it said.

Stock Upgradation by Moody's

Banking:

Moody's Investors Service upgraded the long-term ratings of four Indian financial institutions - Export- Import Bank of India (EXIM India), HDFC Bank, Indian Railway Finance Corporation Limited (IRFC) and State Bank of India (SBI) by a notch to "Baa2".

In the case of HDFC Bank, the rating agency has also upgraded the bank's baseline credit assessment (BCA) and adjusted it to "Baa2" from "Baa3".

Moreover, India's overall sovereign ratings upgradation is positive for banking industry as a whole as the cost of funds will come down with the bond yield falling further.

Oil & Gas:

Moody's has also upgraded the issuer rating for five Government-owned companies in the oil and gas sector to "Baa2" from "Baa3". These entities are Oil and Natural Gas Corporation Ltd (ONGC), India Oil Corporation (IOC), Bharat Petroleum Corp Ltd (BPCL), Hindustan Petroleum Corp Ltd (HPCL), and Petronet LNG Ltd (PLL). The outlook on these ratings have been revised to "stable" from "positive".

At the same time, the foreign currency issuer rating of ONGC has been upgraded to "Baa1" from "Baa2". The outlook is stable.

Infrastructure:

Moody's has taken a number of rating actions on Indian infrastructure government-related issuers (GRIs) too. Moody's has upgraded the ratings of the following GRIs companies: NTPC Limited (NTPC), NHPC Limited (NHPC), National Highways Authority of India (NHAI), Gail (India) Limited (GAIL). It upgraded all four companies rating to "Baa2" from "Baa3" and revised outlook for these companies to "stable" from "positive".

The upgraded ratings reflects the strategic importance of these companies to the country as well as operational financial links with the Government. These entities will receive support from the Government of India in a distress solution. NHAI is responsible for the construction, development and maintenance of national highways in India and upgraded rating ensures that NHAI will continue to get the financial support and operational soundness from the Government. The interest cost would come down and loan funding would be easier than earlier. As a whole, India's overall sovereign ratings upgradation is positive for infra industry, more importantly for the companies which are in heavy debt.

As a whole, we believe, the ratings upgrade is very positive for banks, infrastructure and oil & gas sectors. This upgradation along with a jump in the World Bank's ease-of-doing-business ranking will definitely improves the confidence of global investors.

After Moody's upgraded India's rating, Standard & Poor's (S&P) said India needs to address its weak fiscal position. However, We believe Fitch and S&P will follow the suit with a positive stance or maybe a double upgrade as well. S&P's credit rating for India stands at "BBB-" with stable outlook. Fitch's credit rating for India was last reported at "BBB-" with stable outlook.

Moody's has also upgraded the issuer rating for five Government-owned companies in the oil and gas sector to "Baa2" from "Baa3".

Upgradation on India's sovereign ratings from Fitch and S&P are also likely

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Stock Recommendation	Expected absolute returns (%) over 12 months
Strong Buy	>20%
Buy	between 10% and 20%
Hold	between 0% and 10%
Sell	0 to <-10%
Neutral	No Rating

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