

INDIA-EU TRADE AGREEMENT: A QUICK TAKE

The trade deal reinforces the vision of a “multipolar” global world and strengthens global integration at a time of heightened risk from rising US tariff uncertainties and geopolitical tensions. While implementation and ratification may take time, the deal is expected to cushion the domestic economy against growing global protectionism and rising external headwinds over the medium to long term. This deal may serve as a benchmark for India’s negotiations of future trade deals.

Analysis of State Finances – Story
so Far in FY26



Municipal Bonds in India: Growth
Signals in a High-Potential Market



Petrochemicals: Navigating Through a
Challenging Phase Amidst Competition
from Imports



NOTE FROM **SACHIN GUPTA**

Chief Rating Officer & Executive Director



FTAs and India Inc.'s Moment of Truth

The last few weeks have certainly been very eventful for the Indian economy. Beyond the Union Budget, the announcement of two major and strategically significant Free Trade Agreements (FTAs) with the United States and the European Union has drawn considerable attention. While both agreements have yet to be formally ratified and may take several months for final drafts to emerge, their broader implications are already becoming evident. These FTAs mark an important moment of reckoning for Indian corporates and the economy as a whole.

Three key themes stand out:

Reaffirming India's Importance in the Global Economy

In recent years, delays in trade agreements alongside high tariffs of 50% on exports to the US have started to undermine confidence in India's export competitiveness. These factors have effectively priced Indian goods out of global markets relative to those of other countries, raising doubts about India's capacity to succeed in international export markets. The announcement of these path-breaking FTAs changes that narrative decisively. They reaffirm India's increasing significance in the global economy and indicate that large developed economies view long-term strategic and economic value in deeper engagement with India.

Forcing Competitiveness and Creating Opportunity

The second implication is more structural and, perhaps, more demanding. Indian corporates will now be compelled to defend their domestic market share in sectors such as automobiles, industrial

goods, and processed foods. Increased access for foreign players means that inefficiencies can no longer be masked behind tariff walls. As a result, factors such as cost competitiveness, innovation, quality, and scale will become non-negotiable. Simultaneously, these FTAs unlock significant opportunities. With agreements spanning the US, EU, UK, and other developed markets, Indian companies now enjoy preferential access to economies that represent half of global GDP and have strong purchasing power. This dual pressure—rising domestic competition and expanding international opportunities—will strongly drive operational and strategic transformation.

Importantly, Indian corporates also have a comparative advantage over China in major markets. For example, in the US, the proposed tariff of around 18% on Indian goods is about half the 37% tariff on Chinese exports. Given China's traditionally low-cost structure, driven by scale and manufacturing expertise, this tariff gap offers Indian firms a genuine fighting chance to compete more effectively.

Potential to Kickstart the Private Capex Cycle

Perhaps the most critical long-term impact of these FTAs is the confidence they can instill in Indian businesses to invest. One of the biggest constraints on private capital expenditure has been uncertainty around global trade rules. FTAs provide much-needed clarity on tariff structures and market access, reducing the risk associated with long-gestation investments.

Private capex in India has been sluggish for years despite strong balance sheets and healthy profitability. Now, with a better export outlook, supportive government initiatives such as the Production Linked Incentive (PLI) schemes, ample lending capacity from banks, and robust equity markets for raising capital, the environment is ideal for a revival in private investment. It is arguably one of the best times for Indian corporates to focus on building scale, upgrading technology, and strengthening their integration into global value chains.

Overall, these FTAs are more than just trade deals; they serve as a strategic turning point. They push Indian companies to elevate their standards while providing them with unmatched access to international markets. The way businesses leverage this opportunity will influence India's economic path for years to come.



NOTE FROM

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Government Remains on Fiscal Consolidation Path

The Centre has been on a fiscal consolidation path over the last five years, with the fiscal deficit to GDP ratio reducing from a pandemic high of 9.2% (FY21) to 4.4% (FY26) and budgeted at 4.3% (FY27). While the pace of consolidation has slowed, the Centre is focusing on its medium-term target of debt-to-GDP at 50% (+/-1) by FY31, down from 56% currently. This means the Centre can proceed a little more slowly with fiscal consolidation, provided nominal GDP growth remains healthy, and debt continues to decline.

The Centre achieved its fiscal deficit-to-GDP target of 4.4% in FY26, despite lower tax revenues. Lower gross tax revenues of around Rs 1.9 trillion have been compensated by higher RBI dividend and lower expenditure (mainly revex).

The FY27 fiscal arithmetic also looks achievable. The centre has budgeted gross tax revenue growth of 8%, which seems reasonable given projected nominal GDP growth of 10%. FY27 dividend from RBI and public sector banks is budgeted to be high at Rs 3.2 trillion. Gains from dollar sales and higher interest income are expected to contribute to the high RBI dividend. Interestingly, the disinvestment target (including asset monetisation) has been raised to Rs 800 billion Vs Rs 350 billion estimated for FY26. For the last three years, the Centre has consistently underachieved in disinvestment despite setting a low target (-Rs 500 billion). Thus, the FY27 disinvestment performance remains a monitorable. Going forward, higher asset monetisation and disinvestment receipts remain critical, which can be earmarked for capex.

On the expenditure side, the focus on capex has continued. The centre has budgeted a 12% capex growth to Rs 12.2 trillion in FY27. The total capex (centre + grants + CPSE) is impressive at Rs 22 trillion, up 20% (YoY). The total capex-to-GDP ratio is budgeted to increase to 5.6% in FY27, up from 5.1-5.2% in the previous four years. The share of Centre's capex in total expenditure is budgeted to



increase to 23% in FY27 from a pre-pandemic average of 13% (FY15-19). While focus on roads and railways has continued, defence spending has risen sharply by 17% in FY27 following high growth last year.

General government (Centre+State) debt has declined to 81% (FY25) from 89% (FY21), bucking the global uptrend in government debt. However, general government interest payments (% revenue) remain high at 24% amid a higher cost of capital and a narrow revenue base. Other challenges to India's fiscal landscape include emerging stress in state finances amid the distribution of freebies and lower GST collection. The eighth pay commission recommendations could also strain government finances in FY28. Furthermore, elevated government bond redemptions and higher state borrowings may exert upward pressure on yields.

To conclude, fiscal consolidation would be challenging going forward. While the Centre is showing fiscal discipline, the state governments need to follow suit. Though general government debt-to-GDP is likely to remain on a downward trajectory, the high levels remain challenging for the interest burden. The government should not deviate from its long-term objective of fiscal prudence, even as the going gets tough.

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INDIA-EU TRADE AGREEMENT: A QUICK TAKE

India's economic linkages with the European Union (EU) have deepened over the years, with bilateral merchandise trade between the two rising to USD 136 billion in FY25 from USD 99 billion in FY19. While India's exports to the world grew at a CAGR of 5.9% during FY16-25, exports to the EU have risen by an upbeat 8.7%. India's trade surplus with the EU was recorded at USD 15.9 billion in FY25, up from USD 13.6 billion in FY22.

In FY25, the EU accounted for 17.3% in India's total exports, next to the US (19.8% share). India's exports to the EU have trended upward to a 17.3% share (FY25) from ~14% a decade ago. Within the EU, India's largest export destinations are the Netherlands (5.2% share in total merchandise exports) and Germany (2.4% share). The EU has also

emerged as India's key import partner, with an 8.3% share in total imports, following China (15.8%). India's largest import partner within the EU is Germany (2.6% share in total merchandise imports).

India-EU Trade Deal

India to Gain Greater Access to EU Goods Markets:

Among specific items, engineering goods (export share of 22% to the top EU economies) are set to gain from the preferential market access Vs tariffs as high as 22%. The trade deal also ensures zero duty on 97.5% of India's chemical exports, eliminating duties of up to 12.8%. Among labour-intensive exports, jewellery exports, currently subject to tariffs of up to 4%, are set to gain preferential access to 100% of trade value. Textiles and clothing exports are set to gain zero-duty access across all tariff lines, reducing tariffs by up to 12%. This brings India at par with its key competitors in this segment - Bangladesh, Turkey, Vietnam, etc., that already enjoy duty-free access to the EU market. Moreover, India will gain a 12% duty advantage over China, which has a ~30% market share in the EU's RMG

	Product Share in India's Exports to the EU* (%)	EU's Share in India's Total Product Exports (%)
Engineering Goods	22.0	12.0
Chemicals & Related Products	12.6	12.2
Electronic Goods	11.5	16.9
Agricultural & Allied Products	7.1	8.4
Readymade Garments	5.8	21.8
Gems & Jewellery	4.0	8.0
Textiles (Excluding RMG)	3.4	10.6
Leather & Leather Manufacturers	2.7	36.0

Source: CMIE & CareEdge

*We have considered the top EU economies - the Netherlands, Germany, France, Italy, Belgium and Spain - representing 79% of India's exports to the EU

imports (see CareEdge Report for further details). Leather exports are set to gain from tariff elimination. While leather exports account for just 2.7% in India's total exports to the EU, the sector is of significance since its exports to the EU alone account for 36% of India's total leather exports. However, India has not been exempted from the EU's Carbon Border Adjustment Mechanism (CBAM), which imposes charges on high-carbon goods like steel, cement, fertilisers, and electricity

EU's Gains from Greater Access to Indian Markets:

India will immediately remove tariffs on 30% of EU imports, and overall duties on over 90% of EU goods will be cut or phased out, potentially saving EU exporters about EUR 4 billion annually. Most products that previously faced steep levies - machinery (up to ~44%), chemicals (~22%), and pharmaceuticals (~11%) - will see charges largely disappear. Taxes on EU wines and spirits entering India will also be markedly lowered. The agreement opens India's automotive market to more EU vehicles. Import duties on most cars from the EU priced above EUR 15,000 will be significantly reduced under annual quotas for internal combustion and electric vehicles. However, electric cars will not benefit from the duty cuts for the first five years to safeguard Indian EV manufacturers' investments.

Safeguard for Sensitive Sectors: The deal seeks strategic safeguards for India's sensitive sectors - dairy, cereals, poultry, soymeal, and certain fruits and vegetables. The EU will also retain tariffs on certain sensitive agricultural and food products.

Support for Services Exports: Under the FTA, India has secured broader and deeper commitments from the EU across 144 services subsectors, including IT/ITeS, professional services, education, and other business services. This encompasses a wide range of service sectors and provides Indian service suppliers with a stable, enabling regulatory environment in the EU market. In return, India's market access offer covers 102 service subsectors aligned with key EU priorities, including professional, business, telecommunications, maritime, financial, and environmental services. These commitments will provide EU companies with a predictable, transparent framework for investing in India and delivering innovative services. This is expected to accelerate trade in services.

Easier Mobility of Human Resources: The FTA provides a predictable framework for the temporary entry and stay of professionals, including Business Visitors, Intra-Corporate

Transferees, Contractual Service Suppliers, and Independent Professionals. A comprehensive mobility framework facilitates the movement of employees of Indian companies established in the EU, along with their dependents, across all service sectors. Indian firms supplying services under contract will gain access to 37 subsectors, including IT, business, and professional services. In comparison, Independent Professionals will receive assured market access in 17 subsectors, including IT, R&D, and higher education, expanding opportunities for Indian talent and knowledge-based trade.

Easier Trade and Intellectual Property Protection:

The FTA reinforces intellectual property protections in line with TRIPS, covering copyright, trademarks, industrial designs, trade secrets, plant varieties, and the enforcement of IPRs.

Conclusion

The trade deal reinforces the vision of a "multipolar" global world and strengthens global integration at a time of heightened risk from rising US tariff uncertainties and geopolitical tensions. While implementation and ratification may take time, the deal is expected to cushion the domestic economy against growing global protectionism and rising external headwinds over the medium to long term. This deal may serve as a benchmark for India's negotiations of future trade deals. Broadly, India's and the EU's export items are complementary; however, domestic players in some sectors need to gear up for heightened competition. However, certain aspects, such as the EU's Carbon Border Adjustment Mechanism, remain a key monitorable going forward.



HIGH YIELDS: A POTENTIAL FAULT LINE IN ADVANCED ECONOMIES' DEBT

Advanced Economies have had elevated public debt for two decades now. What has changed more recently is the cost of carrying this debt. In previous episodes of high debt, advanced economies benefited from low borrowing costs, which helped contain debt servicing pressures following the global financial crisis.

As economies pursued monetary tightening in 2022 to address inflationary pressures, yields rose across most advanced economies. Most countries have entered easing cycles since then; however, it has not translated into a meaningful decline in long-term sovereign yields. These persistently high yields reflect a deeper shift in market pricing. Yields are no longer anchored primarily by expectations of policy rates, but increasingly by concerns over fiscal sustainability, growth capacity, and institutional resilience.

The Drivers Behind Persistently Elevated Yields

Fiscal pressures: A defining fiscal challenge for advanced economies is the growing rigidity of their public spending. Unfavourable demographic trends lie at the core of this shift. Further, higher defence and security-related spending, driven by

geopolitical tensions that are no longer episodic, carries tangible fiscal costs.

In addition to expenditure rigidities, elevated debt levels are intensifying fiscal pressures. Advanced-economy public debt stood at 109.1% of GDP in 2024 and is projected to rise to around 120% by 2030, approaching pandemic-era peaks.

Growth concerns: In the past three years (2022–24), average growth in advanced economies was around 2.2%, but projections for 2025–27 point to a slower pace of about 1.7%, with elevated uncertainty clouding the medium-term outlook. This uncertainty reflects near-term cyclical pressures, including weaker global demand, trade fragmentation, and ongoing geopolitical developments.

These pressures are unfolding against longstanding structural headwinds such as ageing populations, modest productivity gains, and subdued private investment, partly due to fiscal crowding-out effects, which are expected to continue weighing on growth prospects in advanced economies.

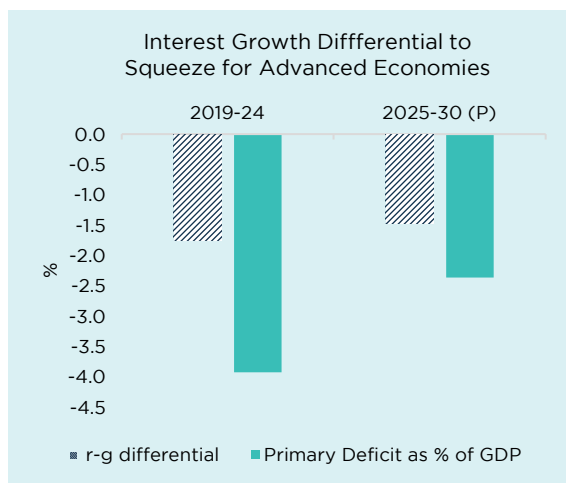
Inability to implement reforms: Meanwhile, the institutional capacity to manage these fiscal and economic headwinds has weakened due to political fragmentation and declining institutional strength. This has weakened the ability to execute policy reforms; therefore, policies involving tax increases or spending controls are increasingly met with public resistance.

The confluence of these challenges has begun to feed into market concerns over future debt dynamics.

Consequently, despite the ongoing cycle of policy rate easing, sovereign yields remain elevated relative to their earlier lows.

With higher-for-longer sovereign yields, advanced economies are expected to face a new set of challenges, including the narrowing of the interest-rate-growth differential ($r-g$) and the rising burden on debt affordability amid widening primary deficits.

Unfavourable interest- growth differential ($r-g$) Debt remains manageable when the effective interest rate on government borrowing is lower than the rate of nominal GDP growth, that is, when the interest-growth differential ($r-g$) is negative. This negative differential can partly or fully offset the impact of primary deficits, thus keeping the debt ratio stable. With persistently high interest rates expected, the ($r-g$) differential is expected to become relatively unfavourable in a few advanced economies, particularly where fiscal deficits are already widened.



Source: IMF, (P) = IMF Projections, CGIL

Widening gap between primary and fiscal deficit, indicating rising interest burden

At the same time, in a higher-for-longer yield environment, borrowing costs are increasing, pushing interest expenditure higher across advanced economies. As a result, the gap between the fiscal and primary balances is set to widen on a more structural basis than in the pre-pandemic period.

How the Current Macro-Fiscal Reality Plays Out Across Advanced Economies

While advanced economies face broadly similar fiscal challenges, their scale and impact vary across countries, reflecting differences in the extent of existing structural fiscal issues, the pace of change in debt dynamics, and institutional strength to absorb fiscal risks. As a

result, the extent to which elevated debt levels translate into sustainability pressures differs materially across sovereigns.

Based on assessments of debt sustainability metrics, advanced economies are grouped into three categories: elevated debt risk, a manageable debt burden supported by fiscal discipline, and a comfortable fiscal position.

Group 1: Elevated Fiscal Risks

Countries such as Italy, the United States, France, the United Kingdom, and Japan fall into a category in which multiple factors are adverse, thereby amplifying vulnerabilities. While these economies retain certain credit strengths, the durability of these buffers will increasingly depend on how quickly weakened fiscal parameters are addressed. For some, the convergence of high debt levels and rising interest expenditure could gradually erode fiscal flexibility over the medium term, unless steps are taken to address them.

Group 2: Manageable Debt Burden Supported by Fiscal Discipline

This group includes economies such as Greece, Spain, Germany and Canada, where structural fiscal risks are present amid elevated or rising debt levels, but are partly mitigated by sustained policy discipline, improving growth dynamics, and supportive institutional frameworks.

Group 3: Comfortable Fiscal Position

This group comprises economies such as the Netherlands, South Korea, Australia and Singapore, which benefit from low debt levels, strong debt affordability, and robust institutional capacity, positioning them well to absorb macroeconomic and financial shocks.

Conclusion

Overall, many advanced economies no longer benefit from the comfortable interest-growth differentials that previously helped stabilise debt dynamics. As financing costs normalise and growth remains modest, this narrowing cushion increasingly constrains fiscal space and reduces tolerance for slippages. Against this backdrop, the fiscal outlook will depend on the ability to rebuild buffers through credible consolidation efforts and to advance reforms that support growth and spending efficiency. The extent to which policymakers can manage this transition will remain a key determinant of debt sustainability and sovereign credit profiles.

ANALYSIS OF STATE FINANCES – STORY SO FAR IN FY26

Our analysis covers the fiscal performance of 22 state governments for April-November 2025. These states together account for ~94% of India's GDP. During 8MFY26, growth in states' aggregate revenue receipts moderated amid a deceleration in tax revenue growth. The moderation in tax growth, however, has been partly offset by healthy double-digit growth in non-tax revenues.

On the expenditure side, growth in states' revenue spending has moderated, while capex has risen by 10.1% in 8MFY26, largely reflecting a favourable base effect from last year. While capex trends so far this year remain broadly in line with historical patterns, capex typically accelerates in the closing months of the fiscal year. A likely increase in capex amid a slowdown in revenues could pose a challenge for the states in meeting their budgeted aggregate fiscal deficit target of 3.3% of GSDP for FY26.

Receipts Performance

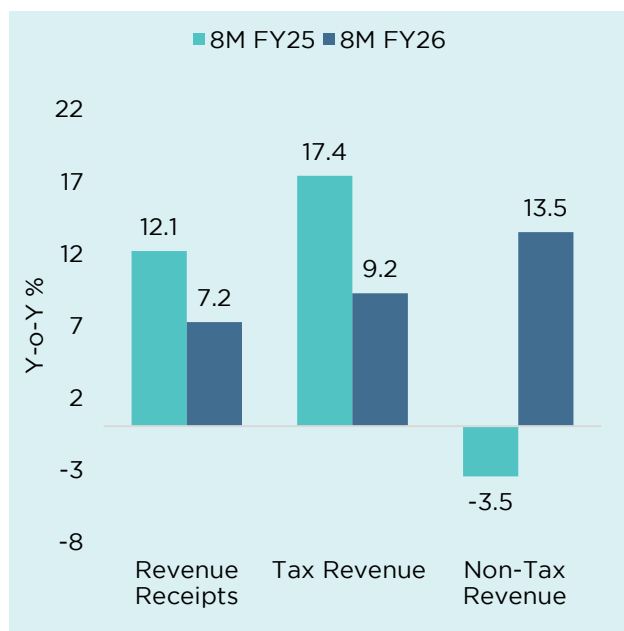
Growth in states' aggregate revenue receipts moderated to 7.2% (y-o-y) in 8MFY26 Vs 12.1% in 8MFY25. Within revenue receipts, the aggregate tax revenues increased by 9.2%, compared to the strong double-digit growth of 17.4% in 8MFY25. Tax collections so far have reached nearly 60% of the full-year budgeted amount, in line with the performance seen a year ago.

Growth in states' GST collections slowed to 5.2% in 8MFY26, Vs ~14% growth in the corresponding period of the last two years. According to an RBI report A one-time negative settlement in April 2025 is expected to have weighed on the SGST

collection. Moreover, the impact of the GST rationalisation implemented from the end of September is expected to weigh on the states' full-year GST collections. Among other taxes, healthy growth in state excise duties (10.3% in 8MFY26 Vs 9.5% in 8MFY25), stamp duty and registration (9.5% Vs 12.7%) and other taxes and duties (12.5% Vs 7.3%) aided the growth in overall tax revenue.

While tax revenues have moderated this fiscal, non-tax revenues increased by 13.5% in 8MFY26 Vs 3.5% contraction in 8MFY25. Mineral-rich states recorded healthy non-tax revenue growth – Chhattisgarh (5.5% in 8MFY26 Vs 11.6% in 8MFY25), Jharkhand (9.8% Vs 4.7%) and Odisha (11.5% Vs 3.1%).

Growth in Revenue Receipts – 8M



Sources: CEIC, CareEdge

Expenditure Performance

States' aggregate revenue expenditure rose 6.9% (y-o-y) during 8MFY26, vs the budgeted growth of 18.5% for the full fiscal. During 8MFY26, states utilised 54.3% of their budgeted revenue expenditure, marginally lower than the 55.8% utilisation recorded in 8MFY25. However, states like Maharashtra, Madhya Pradesh, Uttar Pradesh, and Kerala recorded high revenue expenditure growth in 8MFY26, on the back of prior years' growth.

The moderation in aggregate revenue expenditure can be attributed to the sharp moderation in outgo towards salaries & wages (growth of 2.4% in 8MFY26 Vs 8.4% in 8MFY25), and subsidies (14.5% Vs 32.8%). Spending towards interest payments increased by 9.2% in 8MFY26 Vs 11.5% in 8MFY25.

States' aggregate capex rose 10% in 8MFY26, as against a 5.9% contraction in 8MFY25, as election-related restrictions weighed. States such as Gujarat (48.2% growth), Karnataka (16.6%) and Maharashtra (19%) continued to record healthy capex growth, building on the encouraging performance seen last year. Andhra Pradesh (103%), Assam (35.1%), Haryana (47.9%), Kerala (19.6%), Mizoram (61.9%), Telangana (73.8%), and Uttarakhand (11%) registered strong capex growth on a low base of last year. On the contrary, capex growth in 8M of FY26 and FY25 remained in the negative territory for Uttar Pradesh (-24.7% in 8M FY26), Tamil Nadu (-12.6%), Odisha (-10.1%), Jharkhand (-8.2%), West Bengal (-35.1%), Chhattisgarh (-26.9%) and Himachal Pradesh (-22.5%).

Overall, in 8M FY26, the states have utilised 38.3% of the full-year budgeted capex amount. The capex so far has been broadly in line with historical trends. However, state capex typically accelerates in the closing months of the fiscal year. Capex trends warrant close attention, given states' historical underutilisation of budgeted capex.

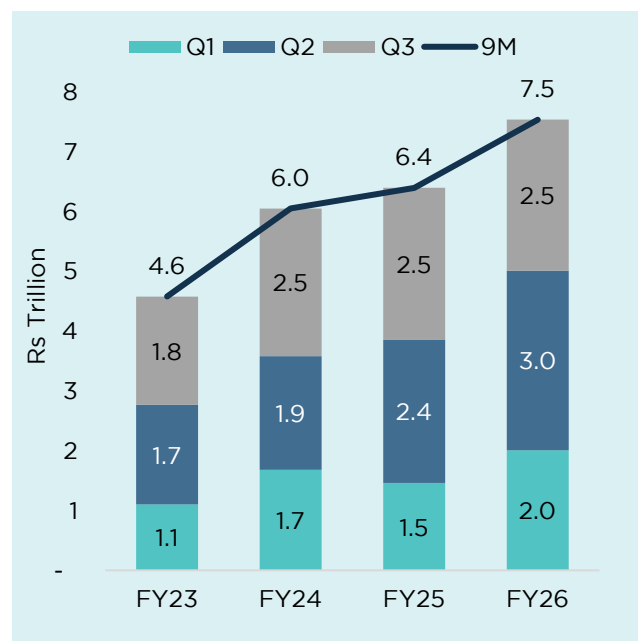
To enhance state capex, the Centre has continued the 50-year interest-free loans under the Scheme for Special Assistance to States for Capital Investment. Under the scheme, the Centre allocated Rs 1.5 trillion in the FY26 Union Budget. In 6MFY26, the centre has already disbursed Rs 500 billion under this scheme and has approved another Rs 700 billion of the Rs 1.5 trillion allocated.

Fiscal Balance & Borrowings

During 8MFY26, states have exhausted ~40.8% of the aggregate fiscal deficit target, as against 40% in 8MFY25. Specifically, the fiscal trajectories of select states remain concerning - Andhra Pradesh (which exhausted 95.7% of the budgeted fiscal deficit amount in 8MFY26 Vs 95.1% in 8MFY25), Himachal Pradesh (72% Vs 67.2%), Kerala (86.2% Vs 64.3%) and Telangana (107.5% Vs 76.8%). At the aggregate level, the states' fiscal deficit is budgeted to be at 3.3% of GSDP for FY26. Given that revenue collections have moderated this year amid slowing tax receipts, the anticipated pickup in capex could pose a challenge for states' fiscal position in FY26.

The states' aggregate fiscal deficit-to-GSDP ratio in FY25 was 3.5%. In FY25, 12 of the 22 states breached the 3% fiscal deficit-to-GSDP limit prescribed by the 13th Finance Commission, while the deficit of 5 states was close to 3%. Overall, against the backdrop of the state's historical fiscal performance and prevailing pressures in the current year, the fiscal position of states is challenging. Given this background, the states have been aggressively tapping market borrowings, borrowing Rs 7.5 trillion in 9MFY26. This is 17.8% higher than the same period last year. Going forward, borrowing requirements are expected to stay high, with states planning to raise Rs 5 trillion in Q4FY26.

Trends in States' Borrowing



Sources: RBI, CareEdge

CROSS-COUNTRY COMPARISON OF BANKING SECTOR IN THE LEADING GLOBAL ECONOMIES

India's Banks Show Improving Strength in a Global Setting

A comparison of banking systems across leading global economies reveals a paradox at the heart of modern finance. Advanced economies boast deep credit penetration, massive balance sheets, and advanced financial markets, yet their banking systems increasingly struggle to generate strong profitability. India, by contrast, presents a structurally different proposition: low credit penetration, high margins, and improving asset quality, together creating a compelling case for sustained and profitable banking expansion.

In most developed economies, banking depth has already peaked. Countries such as the UK, France, China, and Germany report bank credit-to-GDP ratios well above 150%, reflecting decades of financial deepening. However, this maturity has compressed profitability. Net interest margins (NIMs) in these systems remain structurally low due to intense competition, low interest-rate environments, and greater reliance on wholesale funding.

India stands apart. With bank credit equivalent to just about 53% of GDP, the system remains significantly underpenetrated by global standards. Yet, Indian banks deliver the highest margins among major economies. This combination of low penetration and

strong profitability highlights the scale of untapped opportunity within the system. Unlike developed markets, where balance-sheet growth is incremental and returns are hard-won, Indian banks operate in an environment where expanding credit demand can coexist with healthy margins.

This structural advantage strengthens India's appeal as a long-term banking growth market, not only for domestic institutions but also for global banks seeking exposure to high-growth credit ecosystems.

From Balance-Sheet Repair to Growth Readiness

India's banking system has not always enjoyed this position of strength. A decade ago, elevated non-performing assets weighed heavily on profitability and capital. That phase, however, is largely behind us. Today, GNPA and NNPA ratios are at multi-year lows, reflecting sustained recoveries, tighter underwriting standards, and the impact of institutional reforms such as the Insolvency and Bankruptcy Code.

In a global context, Indian banks now sit in a favourable zone, adequately capitalised with improving asset quality. Capital adequacy stands at around 16.4%, comfortably above regulatory requirements and comparable with global peers. While some advanced economies report lower headline NPA ratios, they often operate with thinner capital buffers or higher leverage. India's progress signals a transition from post-crisis clean-up to a phase of growth readiness, where incremental credit risk can be absorbed without destabilising the system.

Scale Gap Remains, Opportunity Endures

Despite these strengths, India's banking system remains small in absolute terms. China's banking assets exceed USD 50 trillion, making its system roughly 15-17 times larger than India's, while the US system is 6-7 times larger. Even Germany's banking sector, operating in a slow-growing economy, is two to three times larger than India's.

This scale gap explains why absolute profits in India remain modest relative to global giants. However, it also reinforces the growth opportunity. As credit penetration gradually increases and financial intermediation deepens, India's banking balance sheet has significant room to expand, supported by favourable demographics, rising formalisation, and increasing demand from retail and MSME segments.

Funding Structures Reflect Structural Differences

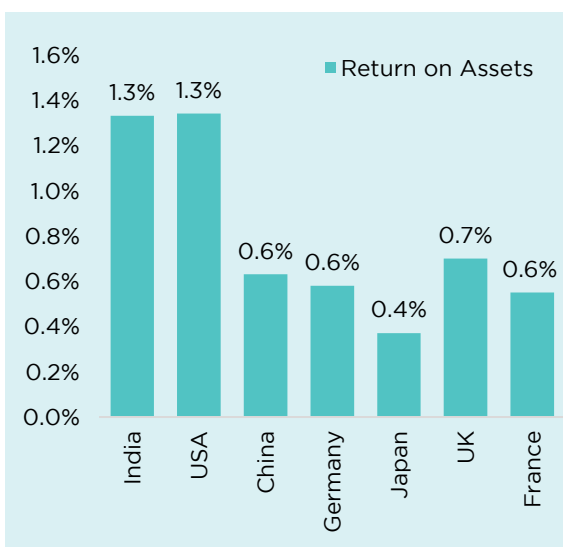
Cross-country differences in funding further illustrate divergent banking models. The UK and Germany operate with higher credit-deposit ratios, reflecting greater reliance on wholesale and cross-border funding. Japan, shaped by decades of risk aversion following its financial crisis, exhibits a structurally low ratio, with deposits consistently outpacing credit demand. India's relatively conservative credit-deposit ratio reflects a deposit-led funding model, supported by stable household savings. This limits excessive dependence on market funding

and contributes to balance-sheet resilience. The US, meanwhile, maintains lower bank credit penetration due to the dominant role of capital markets and non-bank financial intermediaries.

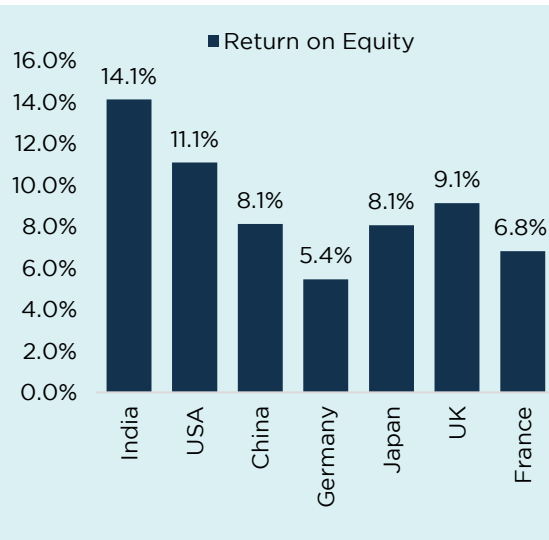
Profitability metrics reinforce India's relative efficiency. While the US and China dominate in absolute profits due to sheer scale, India reports the highest return on assets among peers, driven by strong margins, operating leverage, and digital adoption. Return on equity also remains robust despite lower leverage, highlighting the quality rather than the quantity of growth.

Japan continues to struggle with profitability amid ultra-low interest rates and weak credit demand, while European banks face pressure from regulatory costs and competitive markets. The UK maintains balanced returns through diversified income streams, though volatility and compliance costs remain constraints.

Return on Assets (RoA)



Return on Equity (RoE)



Source: CEIC; Latest respective Fiscal year-end figures, CareEdge Calculations

Conclusion

India's banking system still trails global peers in scale and credit depth, but its structural strengths are increasingly evident. High margins, improving asset quality, adequate capital buffers, and superior risk-adjusted profitability provide a strong foundation for sustainable growth.

As the economy formalises further and credit demand broadens, Indian banks are well positioned to expand without sacrificing stability. The challenge lies in sustaining disciplined risk management and capital allocation. If achieved, India's banks can steadily narrow the gap with global peers—while retaining the advantages that make them distinct.

MUNICIPAL BONDS IN INDIA: GROWTH SIGNALS IN A HIGH-POTENTIAL MARKET



This report is the third sequel to CareEdge Ratings' series on municipal bond issuances in India, following earlier editions published in February 2024 and February 2025.

The growing need for urban infrastructure, coupled with the untapped potential of municipal bonds for financing capital outlay, has triggered a series of reforms in the municipal bond market. SEBI's 2015 revision of the municipal bond framework and the RBI's October 2025 guideline allowing municipal bonds as collateral for repo transactions both aim to enable market development.

FY26 could mark an inflexion point for the muni-bond market, with several first-time issuers entering the market and aggregate issuance at levels not seen since 2018. The municipal bond issuances totalled about Rs 1,000 crore during April-November 2025. Based on planned issuances underway, the likely issuance by the end of FY26 is ~Rs 2000 crore, which compares favourably with the cumulative issuances of approximately Rs 3,000 crore raised over the seven years from 2018 to 2025. Robust profitability, indicated by a 20-25% revenue surplus and a low leverage ratio (debt/revenue surplus below 1x), presents opportunities for additional borrowing. CareEdge Ratings expects municipal corporations to raise additional debt of about Rs 30,000 crore with annual issuance of ~Rs 2500-Rs 3,000 crore per year between FY26 and FY34.

An assessment of around 32 key municipal corporations (covering

metros, tier I, and tier II cities) indicates outstanding debt of approximately Rs 13,500 crore as of March 31, 2025, with muni bonds accounting for less than 20% of this debt. The municipal bond market in India remains small, accounting for only 0.06% of total outstanding corporate bond issuance as of September 30, 2025. In contrast, the U.S. municipal bond market accounts for about 14% of its GDP and 7% of its overall bond market.

The lack of emphasis on capital budgeting policies, a socialistic mindset with an absence of willingness to borrow, a lack of autonomy in decision making, including steps required to augment the revenue base, information asymmetry with improper data management, etc., are some of the key challenges in approaching the capital market by the ULBs.

In the opinion of CareEdge Ratings, a few of the reforms/measures which shall support the municipal bond market include

- i. Granting greater autonomy to Urban Local Bodies (ULBs), strengthening institutional frameworks, and expanding projects under the Public Private Partnership (PPP) model.
- ii. Developing lighthouse cities, which will provide guidance and precedent for others to access the municipal bond market. Such lighthouse cities may propose large issuances rather than small-ticket sizes, which restricts investor appetite and secondary-market development.
- iii. Formulation of Bankruptcy Framework and Debt Management Framework, etc to build creditworthiness, financial transparency and governance capacity of the ULBs.
- iv. Innovative financing mechanisms, along with exploring credit enhancement measures, for uplifting the credit profile of the proposed instrument to gather a wider investor community.



WITH A 2 MILLION BED DEFICIT, INDIA'S HOSPITAL SECTOR POISED FOR 11-12% CAGR GROWTH

India's hospital sector is positioned for sustained medium-term growth, supported by strong structural demand drivers, improving financial health, and a renewed capacity expansion cycle. Post-COVID-19, the sector has undergone meaningful structural shifts, including heightened health awareness, increased elective procedures, gradual price rationalisation, and deeper insurance penetration, which have strengthened demand visibility. The growth outlook is further reinforced by supportive government initiatives such as Ayushman Bharat and the National Health Policy, along with a year-on-year healthcare allocation of ~6% to Rs 1,04,599 crore in the Union Budget FY26.

CareEdge Ratings expects the sector to grow at a healthy CAGR of ~11-12% over the next 3-5 years. Persistently low bed density, rising chronic diseases, an ageing population, increasing insurance coverage, and growing medical tourism underpin long-term demand, with the private sector remaining the key beneficiary amid constrained public healthcare capital expenditure.

Despite accounting for nearly one-fifth of the global population, India's healthcare infrastructure remains underdeveloped, with spending limited to 2-4% of GDP and bed density at ~16 beds per 10,000 population, well below the WHO-recommended norm of 30. This gap is further accentuated by the rural-urban imbalance, with most private hospital capacity concentrated in metros due to stronger paying

profiles. Now, hospital chains are increasingly expanding into Tier-2 and Tier-3 cities, led by lower land and construction costs, underpenetration and volume-led growth.

India's ageing population (the rising 45+ age cohort) is driving increased demand for chronic and specialised healthcare services. Health insurance coverage has expanded materially from ~20 crore individuals in 2014 to ~55 crore in 2024, and is expected to improve further to ~47-50% by FY30, supporting revenue visibility. Additionally, India's cost-efficient, high-quality healthcare ecosystem continues to attract medical tourists, with over 7 lakh arrivals in 2024. Treatment costs in India remain 60-90% lower than in many developed markets, positioning medical tourism as a key revenue driver.

Average Revenue Per Occupied Bed (ARPOB) has grown at an 8-9% CAGR over the past five years (around 7% in FY25) and is expected to grow at 5-6% annually in the near term. Occupancy levels have stabilised at ~62-64% despite capacity additions, supporting robust cash flows. EBITDA margins have improved and stabilised at healthy levels of 21-22%, aided by operating leverage and cost efficiencies.

Strong post-COVID cash accruals have triggered a renewed capex cycle, with planned bed capacity additions of 35-40% over the next 3-5 years to drive volume growth. Despite ongoing capex, credit metrics remain comfortable. Net leverage has improved significantly from ~5.0x in FY19 to ~1.4x in FY25. It is expected to remain comfortable despite marginal moderation as the capex cycle progresses, supported by resilient cash flows and stable profitability.



LIFE INSURANCE PREMIUMS POISED FOR A LONG-TERM GROWTH PATH



The Indian life insurance sector has exhibited sustained long-term growth, with total premiums expanding at a CAGR of around 13% over the past two decades, broadly in line with nominal GDP growth at market prices. In FY25, life insurance continued to dominate the domestic insurance industry, accounting for nearly 74% of total insurance premiums, with aggregate premiums reaching Rs 8.85 lakh crore. While LIC's premiums grew at a CAGR of 9.8% over FY05-FY25, private insurers expanded at a faster pace of 21.7%, reflecting product diversification, innovation, and evolving distribution strategies.

Despite this growth, India remains a structurally underpenetrated market, with life insurance penetration at 2.8% in FY23 and insurance density at \$70, significantly below developed market averages of 5.6% and \$3,182, respectively. This gap highlights substantial headroom for expansion. Based on the CareEdge base-case scenario, life insurance premiums are expected to grow broadly in line with GDP during FY26 and FY27, supported by favourable macroeconomic conditions, regulatory stability, GST exemption on individual life insurance policies, the rollout of Bima Sugam, and increasing demand for protection, non-participating, and annuity products.

Over time, the industry's business mix has shifted meaningfully towards group and single-premium policies. Group premiums reached Rs 2.30 lakh crore in

FY25, growing at a CAGR of 22.3% since FY06, driven by credit-linked covers, pension plans, general annuities, and group gratuity schemes. Individual premiums also expanded steadily to Rs 1.66 lakh crore in FY25, with private insurers outperforming LIC due to broader product offerings and stronger alternative distribution channels. Single-premium policies now account for about 66% of total new business premiums, compared with 43% in FY06. The number of lives covered increased significantly from 14.9 crore in FY15 to about 39.3 crore in FY25, largely led by group insurance. However, most incremental coverage carries low sum assured and limited tenure, leaving mortality and longevity risks inadequately addressed. Pension and annuity penetration remains low, and most insured lives lack a guaranteed post-retirement income stream, underscoring a significant retirement protection gap.

Distribution has evolved from a predominantly agency-led model to a diversified multi-channel framework. Bancassurance has gained prominence, accounting for 32% of individual new business premiums in FY25, while digital and direct channels are increasingly improving access, transparency, and cost efficiency. LIC continues to rely largely on individual agents, whereas private insurers benefit from bank-led distribution.

Overall, the life insurance sector has entered a phase of regulatory stability, with reforms aimed at improving customer outcomes, governance, and transparency. While near-term margin pressures persist due to higher commissions and revised surrender norms, the long-term outlook remains structurally positive, supported by favourable demographics, improving persistency, rising pension and annuity demand, and continued scope to deepen both protection and retirement coverage.



PETROCHEMICALS: NAVIGATING THROUGH A CHALLENGING PHASE AMIDST COMPETITION FROM IMPORTS



Consumption of major petrochemicals, comprising of polymers [including Polypropylene (PP), High Density Polyethylene (HDPE), Low Density Polyethylene (LDPE), Linear Low Density Polyethylene (LLDPE), Polyvinyl Chloride (PVC)], aromatics and elastomers, have witnessed healthy growth in India. Consumption is expected to grow by ~5% in FY26, with key petrochemical consumption volumes projected at ~29 mn tonnes.

Strong consumption growth, the absence of domestic capacity additions, and cheaper imports driven by large global capacity expansion have led to a sharp surge in imports over FY23-FY24, thereby reducing the domestic industry's capacity utilisation under competitive pressures. Imports in FY25 declined primarily due to lower polyethylene imports upon the imposition of the Quality Control Order (QCO) from January 2024. For FY26, import volumes are expected to remain at a level similar to FY25, given that no significant increase in imports has been observed through October 2025. The domestic market remains dependent on imports of key petrochemical products. About three-fourths of the PVC requirement is met through imports while about fifth of PP and Polyethylene requirement is met through imports.

Against the backdrop of high import dependence and growing consumption, domestic players have outlined large-capacity expansion plans, particularly in PVC and PP. However, given the long capex timeline and subsequent ramp-up, India is expected to remain reliant on imports in the near term to meet domestic requirements. In contrast, large-capacity expansion is

expected to gradually reduce the country's import dependency only in the medium term.

Spreads of key petrochemical products increased substantially in FY21-FY22, driven by strong pandemic-fuelled demand for plastics. However, tapering demand thereafter, coupled with oversupply from significant capacity additions in China, led to a substantial decline in spreads, which have remained subdued for the last three and a half years, ending H1FY26. The recent decline in crude oil prices has provided some respite, with a marginal improvement in operating profitability margin for Indian petrochemical players in H1FY26. Maintaining it and gradually improving it would be critical.

India's growth in petrochemical consumption is expected to remain robust at 6-7% p.a. in the medium term, driven by economic expansion and downstream product demand. Both public and private-sector companies have developed aggressive plans to increase their petrochemical capacity. Polypropylene capacity is expected to rise 1.8x between FY25-FY30, surpassing the envisaged demand growth of 1.4x, which could largely eliminate import dependence by FY30. However, improving cost competitiveness, leading to recovery in spreads and thereby earning reasonable returns on their investments, would remain key monitorable for domestic petrochemical players," said Rabin Bihani, Associate Director, CareEdge Ratings.

"Prices and spreads in the domestic petrochemical sector are expected to remain weak in the near term due to global oversupply. While there has been marginal recovery in spreads in H1FY26 which could support ~200 bps improvement in EBITDA margin in FY26, sustained recovery and achievement of optimum operating profitability would hinge more on their cost competitiveness, global demand-supply scenario and need-based support from the Government given sizeable global capacity additions especially by China, which has impacted the profitability of Indian manufacturers for an extended period of time," said Hardik Shah, Director, CareEdge Ratings.



HEAT MAP AND PROJECTION TABLE

		Jan-25	Feb-25	Mar-25	Apr-25	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25	Jan-26
PMI-M	Unit	57.7	56.3	58.1	58.2	57.6	58.4	59.1	59.3	57.7	59.2	56.6	55.0	55.4
PMI-S	Unit	56.5	59.0	58.5	58.7	58.8	60.4	60.5	62.9	60.9	58.9	59.8	58.0	58.5
GST Collections	Rs lakh crore	1.8	1.8	2.0	2.4	2.0	1.8	2.0	1.9	1.9	2.0	1.8	1.7	1.9
E-Way Bill	Crore	11.8	11.2	12.5	11.9	12.3	11.9	13.2	12.9	13.2	12.7	13.0	13.8	13.7
Air Passenger Traffic	Crore	3.7	3.5	3.6	3.6	3.5	3.4	3.2	3.3	3.2	3.5	3.8	3.6	
PV Sales	Lakh	4.1	3.9	4.1	3.6	3.7	3.5	3.7	3.6	4.0	4.7	4.4	4.2	
2-3-Wheeler Sales	Lakh	19.9	18.6	21.1	19.0	21.2	20.5	21.1	23.8	27.2	27.6	25.3	21.1	
Tractor Sales	Lakh	0.7	0.7	0.9	0.9	1.0	1.2	0.7	0.7	1.5	1.7	1.0	0.8	
IIP	y-o-y%	5.2	2.7	3.9	2.6	1.9	1.5	4.3	4.1	4.6	0.5	7.2	7.8	
Core Sector	y-o-y%	5.1	3.4	4.5	1.0	1.2	2.2	3.7	6.5	3.3	-0.1	2.1	3.7	
Power Consumption	y-o-y%	2.7	-0.8	6.7	2.2	-4.9	-1.5	2.1	4.3	3.2	-6.0	-0.8	6.1	3.9
Petroleum Consumption	y-o-y%	3.0	-5.2	-3.1	0.2	1.1	0.5	-4.4	4.8	7.0	-1.5	2.8	5.3	
Outstanding Bank Credit - Total	y-o-y%	11.4	11.0	11.0	10.3	9.0	9.5	10.0	10.0	10.4	12.5	11.5	14.5	
Capital Goods Import	y-o-y%	15.5	-0.5	8.6	21.5	14.3	2.6	12.2	-1.3	10.1	8.7	13.1	13.2	
Merchandise Exports	y-o-y%	-2.7	-10.8	0.8	-3.8	-1.2	-1.3	13.3	5.8	6.1	-12.4	19.3	1.8	

Indicator	FY18	FY19	FY20	FY21	FY22	FY23	FY24	FY25	FY26 Forecast
Gross Domestic Product (y-o-y%)	6.8	6.5	3.9	-5.8	9.7	7.6	9.2	6.5	7.4 #
CPI Inflation (y-o-y%)	3.6	3.4	4.8	6.2	5.5	6.7	5.4	4.6	2.1
Fiscal Deficit (As % of GDP)	3.5	3.4	4.6	9.2	6.8	6.4	5.6	4.8	4.4
Current Account Balance (As % of GDP)*	-1.8	-2.1	-0.9	0.9	-1.2	-2.0	-0.7	-0.6	-1.0
10-Year G-Sec Yield (%) (Fiscal year-end)	7.3	7.5	6.1	6.3	6.8	7.3	7.1	6.6	6.4-6.6

As per the first advanced estimates; *(-) Deficit / (+) Surplus; Fiscal deficit data for FY26 is revised estimate.

About Us

CareEdge is a knowledge-based analytical group offering services in Credit Ratings, Analytics, Consulting and Sustainability. Established in 1993, the parent company CARE Ratings Ltd (CareEdge Ratings) is India's second-largest rating agency, with a credible track record of rating companies across diverse sectors and strong position across the segments. The wholly-owned subsidiaries of CareEdge Ratings are (I) CARE Analytics & Advisory Private Ltd, (II) CARE ESG Ratings Ltd, and (III) CareEdge Global IFSC Ltd. CareEdge Ratings' other international subsidiary entities include CARE Ratings (Africa) Private Ltd in Mauritius, CARE Ratings South Africa (Pty) Ltd, and CARE Ratings Nepal Ltd. For more information: www.careedge.in.

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