August 16, 2023

RBL Bank Limited: Ratings reaffirmed; Rating withdrawn for matured/redeemed instrument

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Basel III Tier II Bonds	70.00	70.00	[ICRA]AA- (Stable); reaffirmed
Basel III Tier II Bonds	330.00	-	[ICRA]AA- (Stable); reaffirmed and withdrawn
Fixed Deposit	-	-	[ICRA]AA- (Stable); reaffirmed
Short-term Fixed Deposit	-	-	[ICRA]A1+; reaffirmed
Certificates of Deposit	6,000.00	6,000.00	[ICRA]A1+; reaffirmed
Total	**6,400.00**	**6,070.00**	

**Instrument details are provided in Annexure I*

Rationale

The ratings reaffirmation factors in the relative improvement in RBL Bank Limited's (RBL) profitability on the back of the moderating credit costs and the steady growth in the overall deposit base. The ratings also factor in the bank's comfortable capital position and adequate liquidity. While the net profitability levels have seen a relative improvement, the sub-optimal operating profitability remains weighed down by the elevated cost of funds as well as the high operating costs. Furthermore, despite the steady growth in the overall deposit base and the share of retail deposits, the dependence on bulk deposits remains relatively high, leading to a higher cost of funds compared to the average for private sector banks (PVBs), as well as elevated depositor concentration levels. Going forward, RBL's ability to build a more granular and stable deposit base at competitive rates will be a key driver of its scale of operations. Its ability to shift towards secured granular retail assets will be key for a sustained improvement in its asset quality and profitability.

The long-term rating remains constrained by the high share of the unsecured retail loan book (largely credit cards and microfinance), which witnessed severe weakening in the asset quality and profitability pressures during the Covid-19 pandemic. Given the inherent nature of these segments, RBL will remain vulnerable to the credit risks arising from this portfolio, although the high-yielding unsecured retail book and comfortable capital position will be protective factors. Additionally, the sub-optimal operating profitability could limit the bank's ability to absorb credit costs in the event of stress.

The Stable outlook factors in ICRA's expectation that the bank will be able to maintain a comfortable capitalisation and solvency position, although the increasing share of the unsecured retail book is a concern. This book is likely to reduce only over the medium term as RBL expands its secured retail product offerings.

ICRA has withdrawn the rating assigned to the Rs. 330.00-crore Basel III Tier II Bonds as these have been fully redeemed with no amount outstanding against the same. The rating was withdrawn in accordance with ICRA's policy on the withdrawal of credit ratings (click here for the policy).

Key rating drivers and their description

Credit strengths

Comfortable capital position – While RBL's profitability has improved from past levels, the growth in the loan book and risk-weighted assets led to capital consumption. Nonetheless, the Tier I ratio remained comfortable at 15.05% as on June 30, 2023 (16.00% as on June 30, 2022). Amid the weak profitability/losses in the recent past, the capitalisation profile was supported by the equity capital raise of Rs. 1,566 crore in FY2021 and Rs. 2,701 crore in FY2020. The bank also raised $100 million in May

2022 (Tier II capital), which supported an increase in the capital-to-risk weighted assets ratio (CRAR) to 16.68% as on June 30, 2023 (17.51% as on June 30, 2022).

Going forward, RBL has guided towards further improvement in internal capital generation although the same is contingent on the credit costs remaining within the guided range for FY2024. While the improvement in the return indicators is likely to be gradual, the overall capital cushions as well as the solvency levels are expected to remain better than the negative rating triggers.

Stable deposit base, although share of bulk deposits remains high – Deposit accretion continued at a steady pace with the overall deposit base growing 8.1% YoY to Rs. 85,636 crore as on June 30, 2023, although it trailed the much stronger 21.3% YoY growth in advances during this period (advances stood at Rs. 73,087 crore). However, advances growth was supported by the higher on-balance sheet liquidity maintained in addition to incremental deposit mobilisation.

RBL has been gradually increasing the share of retail deposits, but the share of bulk term deposits (>Rs. 2 crore) remains high (36.8% of total deposits as on June 30, 2023 vs 41.8% as on June 30, 2022). The high share of bulk deposits leads to elevated depositor concentration levels with the share of the top 20 depositors at 16.2% as on March 31, 2023 (16.6% as on March 31, 2022 and 15.3% as on March 31, 2021). This, along with the lower share of current account savings account (CASA) at 37.3% as on June 30, 2023 (36.0% as on June 30, 2022), in relation to the PVB average, led to the higher cost of interest-bearing funds at 4.97% in FY2023 compared to 4.05% for PVBs. The overall differential in the cost of funds is likely to remain high as efforts to granularise the liability profile through branch network expansion will bear fruit over the medium to long term. This will also be key for protecting the bank's profitability while growing its presence in other segments with relatively lower risk.

Credit challenges

Asset quality remains monitorable – ICRA notes that the high-yielding unsecured retail segments (primarily comprising credit cards and microfinance) have been a source of asset quality challenges, which intensified during the pandemic. The pandemic-induced slippages in these segments mainly led to the higher fresh non-performing advances (NPA) generation of 4.65% in FY2023 (5.5-6.9% during FY2021-FY2022), which has since moderated to 3.20% (on an annualised basis) in Q1 FY2024.

Despite the asset quality stress, the headline asset quality numbers, i.e. gross and net NPAs, witnessed relatively less deterioration because of the sizeable write-offs done by the bank. As a result, RBL's overall credit costs remained elevated, which impacted its profitability and return metrics. As the impact of the pandemic waned, the share of the standard restructured book (1.1% of the standard advances as on June 30, 2023) along with overdue advances in the retail segments and the corporate book internally rated BB & below, in relation to RBL's capital, moderated to much lower and manageable levels. Nevertheless, the residual vulnerable book will remain a monitorable.

Notwithstanding the reduction in the vulnerable book, the share of unsecured retail loans remained high at 33.1% of overall loans as on June 30, 2023 and will remain susceptible to any material weakening in macro-economic factors, including elevated commodity/input prices, as well as higher servicing costs as the rise in interest rates could pressurise a certain set of borrowers. The ability to keep slippages at lower levels will be key for an improvement in the bank's asset quality and profitability metrics.

Sub-optimal core operating profitability; improvement key for increasing overall profitability – RBL's changing business mix in recent years, involving its growing presence in unsecured retail segments, initially supported an improvement in its operating profitability. However, operating expenditure/average total assets (ATA) remained high at 4.4% in Q1 FY2024 (2.9-4.3% during FY2021-FY2023) due to the significant operational intensity in these segments. High operating costs, muted growth in the loan book and excess liquidity during the pandemic remained a drag on the profitability, with the core operating profitability moderating to 1.8% of ATA in FY2023 from 3.0-3.1% during FY2020-FY2021 (loss of -0.59% of ATA in FY2022). With the improvement in loan growth and reduction in surplus liquidity, the operating profit grew to 2.1% of ATA in Q1 FY2024.

Furthermore, high slippages during FY2020-FY2023 (first due to corporate book slippages, followed by a sharp spike in slippages induced by the pandemic in the unsecured retail segments) resulted in elevated credit costs, which led to the weakening of the net profitability and the return on assets (RoA) during this period. However, credit costs moderated to 0.9% of ATA during FY2023-Q1 FY2024 (2.4-2.5% during FY2021-FY2022), resulting in an improvement in the RoA to 1.0% of ATA in

Q1 FY2024 (0.8% in FY2023) against losses reported in FY2022. The ability to improve the operating leverage and control credit costs will be key for increasing the operating profitability and sustaining the improvement in internal capital generation.

Environmental and social risks

While banks like RBL do not face material physical climate risks, they are exposed to environmental risks indirectly through their portfolio of assets. If the entities or businesses, to which banks and financial institutions have an exposure, face business disruptions because of physical climate adversities or if such businesses face climate transition risks because of technological, regulatory or customer behaviour changes, it could translate into credit risks for banks. However, such risks are not material for RBL as it benefits from adequate portfolio diversification. Further, the lending is typically short-to-medium term, allowing it to adapt and take incremental exposure to businesses that face relatively fewer downside environmental risks.

With regard to social risks, data security and customer privacy are among the key sources of vulnerability for banks as material lapses could be detrimental to their reputation and invite regulatory censure. RBL has not faced such lapses over the years, which highlights its sensitivity to such risks. It is seen to be operating responsibly in terms of its selling practices with no instances of fines being imposed by the regulatory authorities because of misconduct. Customer preferences are increasingly shifting towards digital banking, which provides an opportunity to reduce the operating costs. RBL has been at the forefront of making the requisite investments to enhance its digital interface with its customers. While it contributes to promoting financial inclusion by lending to the under-served segments, its lending practices remain prudent, as reflected in the healthy asset quality numbers in this segment compared with its peers.

Liquidity position: Adequate

Despite the excess statutory liquidity ratio (SLR) of ~14% of net demand and time liabilities (NDTL) on the fortnightly reporting date of May 19, 2023 (over the regulatory minimum of 18%), the high share of bulk deposits tempers the liquidity profile. The daily average liquidity coverage ratio was 129% in Q1 FY2024. The excess SLR can be utilised to avail liquidity support from the Reserve Bank of India (RBI; through repo) apart from the marginal standing facility in case of urgent liquidity needs. The bank's ability to maintain a high rollover rate of deposits and improve the granularity of the deposit base in the future will remain a key factor for sustaining liquidity.

Rating sensitivities

Positive factors – ICRA could revise the outlook to Positive or upgrade the rating if there is a sustained improvement in the granularity of the liability profile along with a decline in the cost of funds in relation to the sector. The bank's ability to maintain the capital cushions above 3% of the Tier I regulatory levels (9.5% including capital conservation buffers) and the RoA above 1.5% on a sustained basis will be a key positive factor.

Negative factors – ICRA could assign a Negative outlook or downgrade the ratings if there is a deterioration in the asset quality or capital position, leading to the weakening of the solvency profile with net NPA/core equity of more than 25% on a sustained basis. Further, a sustained RoA of less than 1.0% and/or a decline in the capital cushions to less than 2% in relation to the Tier I regulatory levels on a sustained basis will remain negative triggers. Moreover, a material weakening in the bank's liability franchise, impacting its resource profile, will be a negative factor.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA's Rating Methodology for Banks and Financial Institutions Policy on Withdrawal of Credit Ratings Rating Approach – Consolidation
Parent/Group support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the standalone financials of RBL. However, in line with ICRA's limited consolidation approach, the capital requirement of the key subsidiary of the bank (i.e. RBL FinServe Limited) has been factored in.

About the company

Maharashtra-based RBL Bank Limited is a private sector bank established in 1943. It received the status of a scheduled commercial bank in 1959. The bank underwent a management change in FY2011, following which its corporate office was shifted to Mumbai. Apart from the management change, RBL's shareholding changed in FY2011 with equity infusions from various private equity funds. From its erstwhile name of Ratnakar Bank Limited, it was renamed RBL Bank Limited in mid-2014. It was listed on the BSE and NSE with its initial public offering (IPO) in August 2016. As on June 30, 2023, RBL had 520 branches, 298 banking outlets, 1,115 business correspondent (BC) branches (including banking outlets) and 414 ATMs.

Key financial indicators (standalone)

RBL Bank Limited	FY2022	FY2023	Q1 FY2023	Q1 FY2024
Net interest income	4,027	4,451	1,028	1,246
Profit before tax	77	1,181	276	381
Profit after tax	(75)	883	201	288
Net advances (Rs. lakh crore)	0.60	0.70	0.60	0.73
Total assets (Rs. lakh crore)	1.06	1.16	1.08	1.18
CET	16.21%	15.25%	16.00%	15.05%
Tier I	16.21%	15.25%	16.00%	15.05%
CRAR	16.82%	16.92%	17.51%	16.68%
Net interest margin / ATA	3.89%	4.01%	3.84%	4.26%
Net profit / ATA	-0.07%	0.79%	0.75%	0.98%
Return on net worth	-0.59%	6.74%	6.32%	8.40%
Gross NPAs	4.40%	3.37%	4.08%	3.22%
Net NPAs	1.34%	1.10%	1.16%	1.00%
Provision coverage excl. technical write-offs	70.44%	67.33%	72.52%	68.95%
Net NPA/ Core capital	6.56%	5.95%	5.57%	5.51%

Source: RBL Bank Limited, ICRA Research; Amount in Rs. crore unless specified otherwise; All calculations as per ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information

Disclosure: A member of the board of directors of ICRA Limited is also an Independent Director on the board of directors of RBL. This Director was not involved in any of the discussions and processes related to the rating(s) of the instrument(s) mentioned herein.

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years					
		Type	Rated Amount	Amount Outstanding as on Aug 07, 2023	Date & Rating in FY2024	Date & Rating in FY2023		Date & Rating in FY2022		Date & Rating in FY2021
			(Rs. crore)	(Rs. crore)	Aug 16, 2023	Sep 14, 2022	Jun 09, 2022	Feb 14, 2022	Dec 31, 2021	Feb 25, 2021
1	Certificates of Deposit	Short term	6,000.00	2,000.00^	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
2	Short-term Fixed Deposits	Short term	-	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
3	Basel III Tier II Bonds	Long term	70.00	-^	[ICRA]AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA-&	[ICRA] AA-&	[ICRA] AA-&	[ICRA] AA-(hyb) (Stable)
4	Basel III Tier II Bonds	Long term	330.00	-	[ICRA]AA- (Stable); withdrawn	[ICRA] AA- (Stable)	[ICRA] AA-&	[ICRA] AA-&	[ICRA] AA-&	[ICRA] AA-(hyb) (Stable)
5	Fixed Deposits	Long term	-	-	[ICRA]AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA-&	MAA&	MAA&	MAA (Stable)

& Rating Watch with Developing Implications; ^ Balance amount yet to be placed
Note: In compliance with the circular issued by the Securities and Exchange Board of India (SEBI) on July 16, 2021 for standardising the rating scales used by credit rating agencies, ICRA has discontinued its practice of affixing the (hyb) suffix alongside the rating symbols for hybrid instruments

Complexity level of the rated instrument

Instrument	Complexity Indicator
Basel III Tier II Bond	Highly Complex
Fixed Deposit	Very Simple
Short-term Fixed Deposit	Very Simple
Certificates of Deposit	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE976G08064	**Basel III Tier II Bonds**	Sep 27, 2016	10.20%	Apr 15, 2023	330.00	[ICRA]AA- (Stable); withdrawn
NA	**Basel III Tier II Bonds**	Yet to be placed	-	-	70.00	[ICRA]AA- (Stable)
NA	**Certificates of Deposit**	Yet to be placed	-	7-365 days	4,000.00	[ICRA]A1+
INE976G16NF0	**Certificates of Deposit**	Jul 11, 2023	7.75%	Sep 25, 2023	1,250.00	[ICRA]A1+
INE976G16NE3	**Certificates of Deposit**	Jun 15, 2023	7.38%	Oct 06, 2023	750.00	[ICRA]A1+
NA	**Short-term Fixed Deposits**	NA	NA	NA	-	[ICRA]A1+
NA	**Fixed Deposits**	NA	NA	NA	-	[ICRA]AA- (Stable)

Source: RBL Bank Limited; CD outstanding as on August 07, 2023

Key features of rated debt instruments

The servicing of the Basel III Tier II Bonds is expected to absorb losses once the point of non-viability (PONV) trigger is invoked by the RBI. The Basel III Tier II Bonds have equity-like loss-absorption features. Such features may translate into higher loss severity vis-à-vis conventional debt instruments.

Annexure II: List of entities considered for limited consolidated analysis

Company Name	RBL Bank Ownership	Consolidation Approach
RBL FinServe Limited	100%	Limited Consolidation

Source: RBL Bank Limited

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