RBL Bank Limited

February 08, 2019

Summary of rating action

Instrument*	Previous Rated Amount(Rs. crore)	Current Rated Amount(Rs. crore)	Rating Action
Basel III Compliant Tier II Bond Programme	800.00	800.00	[ICRA]AA- (hyb) (stable); reaffirmed
Medium-term Fixed Deposit Programme	-	-	MAA (stable); reaffirmed
Short-term Fixed Deposit Programme	-	-	[ICRA]A1+; reaffirmed
Certificate of Deposits Programme	6,000.00	6,000.00	[ICRA]A1+; reaffirmed
Total	**6,800.00**	**6,800.00**	

** Instrument details are provided in Annexure-1*

Rationale

The ratings factor in RBL Bank Limited's (RBL) steadily improving scale of operations and profitability. Despite the rising costs of funds, profitability was supported by a steady increase in the benchmark lending rates as well as the changing mix of advances towards high-yielding assets like microfinance loans and the credit card business. It was also supported by the increasing share of non-interest income though this was partially offset by increasing operating costs associated with the expansion of new businesses and branch infrastructure. With high growth in assets, despite strong growth in retail liabilities as well as current and savings account (CASA) deposits, dependence on bulk deposits remains high, thereby leading to higher cost of funds compared to the average for private banks (PVBs). The recent tightening in liquidity conditions has led to a higher increase in the cost of funds for the bank compared to the PVB average though the same was comparable to peers. The deposit concentration towards top depositors has been improving and remains a positive. Despite the high share of bulk deposits, RBL's liquidity remains comfortable with 1-year structural liquidity gaps of -2.36% of outflows and a comfortable liquidity coverage ratio of 119% as on December 31, 2018. This is, in turn, supported by the increasing share of non-callable deposits and shorter maturity profile of assets.

Notwithstanding the improving profitability, the increasing share of microfinance loans, where the borrower profile is vulnerable to economic shocks, and unsecured credit cards advances increases RBL's vulnerability to credit risk. This is partially offset by strong collection efficiencies in microfinance loans originated post demonetisation and satisfactory asset quality in the credit card segment though the same remains monitorable. In the corporate loan segment, the reducing concentration of advances to the top 20 borrower groups is a positive with the same declining to 21% of the total exposures and 217% of Tier I capital as on March 31, 2018 from 29% and 319%, respectively, as on March 31, 2016. However, the delinquencies in this segment also remain a monitorable as the seasoning improves. The ratings remain supported by RBL's comfortable capitalisation levels and its experienced senior management team. With estimated growth in assets, the bank would need to raise capital in the next one year. It is comfortably placed in relation to the size of capital requirements and the market capitalisation with a demonstrated track record of raising capital to maintain the capital cushion.

Outlook: Stable

The Stable outlook factors in ICRA's expectations that the bank will continue maintaining strong asset quality while improving the diversity in the asset and liability profile. Further, supported by the steady growth in core earnings, ICRA expects continued improvement in the profitability levels. Though the bank will need to raise capital during the next one year to support growth, it is well-placed in terms of its ability to raise capital. The ability to diversify the mix of assets and liabilities, while it maintains a comfortable asset quality and capitalisation, will remain a key rating positive. Conversely, a sharp deterioration in the asset quality as the loan book seasons, thereby leading to a decline in profitability, or an increase in the concentration of exposures or liabilities will be rating negatives. Any weakening in RBL's ability to raise capital, coupled with a decline in the capital cushion over the regulatory requirements, will be another key rating negative.

Key rating drivers

Credit strengths

Steadily improving scale of operations – The bank's loan book grew by 35% YoY to Rs. 40,268 crore as on March 31, 2018 and further by 35% YoY to Rs. 49,893 crore as on December 31, 2018. This is in line with RBL's medium-term plans of growing the loan book at a CAGR of 30-35% till FY2020. Within the loan book, the share of non-wholesale advances stood at 43% as on December 31, 2018 (38% as on December 31, 2017). Growth in non-wholesale advances was supported by retail assets (YoY growth of 56%) and micro banking (up 46% YoY), which was driven by the business correspondent (BC) branch expansion. Within retail assets, RBL witnessed growth in its credit cards portfolio (9% of the overall book as on December 31, 2018), which is seeing good traction with the bank having cards of a little less than 1.5 million and a run rate of ~90,000 cards per month. Within the wholesale segment, RBL largely caters to the short-term working capital requirements of corporate customers. Of the total loan book, 64% of the advances were for a tenure of less than 1 year while 84% was in the less than 3-year tenure bracket as on December 31, 2018. Of the total portfolio, 67% was secured as on December 31, 2018 (68% as on December 31, 2017). The unsecured portfolio includes loans to microloan borrowers, credit cards, business loans, as well as bank lines for certain highly rated large corporate borrowers. With the growth in RBL's portfolio expected to be higher than the sector average, ICRA expects RBL's market share to improve steadily.

Capitalisation profile remains comfortable – The bank reported comfortable capitalisation with Tier I and CRAR, as a percentage of risk weighted assets (RWAs), of 12.5% and 13.8%, respectively, as on December 31, 2018 (14.1% and 15.9%, respectively, as on December 31, 2017). The bank last raised capital through a preferential issue of Rs. 1,680 crore in August 2017, which helped in boosting the capitalisation. Earlier in August 2016, RBL had raised Rs. 832 crore through its initial public offering (IPO) and Rs. 488 crore in FY2016 from investors prior to its IPO listing. The solvency remained strong and was better than the industry average with net NPAs/net worth of 4.9% as on December 31, 2018 (5.5% as on December 31, 2017). With quarterly capital consumption of ~40-45 bps of Tier I, the bank would need to raise capital in the next one year, as per ICRA's assessment. In ICRA's view, the bank is comfortably placed in relation to the size of capital requirements and market capitalisation with a demonstrated track record of raising capital to maintain the capital cushion.

Steady improvement in profitability – The yield on advances increased to 10.6% in 9M FY2019 (9.8% in FY2018) with an increase in the MCLR and the change in the portfolio mix towards higher-yielding non-wholesale advances. This was partially offset by the increase in the cost of interest-bearing funds to 6.1% in 9M FY2019 (5.7% in FY2018) due to the tighter liquidity conditions and higher interest rates. NIMs improved to 3.6% in 9M FY2019 (3.2% in FY2018). Higher NIMs and increasing non-interest income of 1.9% of ATA in 9M FY2019 (1.6% in FY2018) translated into improving operating profitability of 2.6% of ATA in 9M FY2019 (2.1% in FY2018) despite the increase in operating costs (2.89% of ATA in 9M FY2019 vis-à-vis 2.72% in FY2018) associated with the expansion of new businesses and branch infrastructure. Improved core profitability was partially offset by higher credit provisions in the microfinance segments of 0.9% of ATA in 9M FY2019 (0.7% in FY2018). This led to a limited improvement in profit after tax (PAT)/ATA to 1.2% in 9M FY2019 from 1.1% in FY2018. The cost of funds for the bank is expected to increase due to the rise in interest rates and the continued reliance on wholesale funding in the backdrop of high growth plans. However, the increase in the share of high-yielding assets and the positive impact of revision in the MCLR is expected to offset the increase in the cost of funds. ICRA expects the NIMs and RoA to continue improving, driven by the improving scale of operations, though they will remain exposed to asset quality shocks.

Comfortable asset quality – With slippages in microfinance loans (part of the Development Banking and Financial Inclusion (DB&FI) segment) post demonetisation and higher slippages in the agri portfolio, the bank's asset quality weakened with gross NPAs (GNPAs) increasing to 1.40% as on March 31, 2018 (1.20% as on March 31, 2017). The asset quality has stabilised with GNPAs of 1.38% as on December 31, 2018, as incremental movement to higher overdue buckets in microloans has reduced and overdues have stabilised. With a provision cover ratio (PCR) of 48.6%, the net NPAs stood at 0.72% as on December 31, 2018 (PCR of 38% and net NPA of 0.97% as on December 31, 2017). The bank's standard restructured assets stood limited at 0.09% of the total advances as on December 31, 2018 (0.18% as on December 31, 2017). RBL's security receipts were also limited at 0.05% of the total advances as on December 31, 2018. Moreover, the bank does not have any exposure to the accounts identified by the Reserve Bank of India (RBI) for insolvency proceedings. It has no SDR, S4A or 5/25 refinancing. With limited vulnerable accounts, RBL's asset quality is expected to remain stable. However, the increase in exposure to MFIs and credit cards exposes the bank to credit risk.

Comfortable liquidity – The bank's liquidity remains comfortable with 1-year negative structural liquidity gaps of 2.36% of outflows as on December 31, 2018. RBL's comfortable liquidity coverage ratio (119% as on December 31, 2018 against the regulatory requirement of 90% as on January 01, 2018 and 100% as on January 01, 2019) provides further comfort. This is, in turn, supported by the increasing share of non-callable deposits and shorter maturity profile of assets.

Credit challenges

Despite improvement, resource profile remains concentrated – Notwithstanding the gradual improvement, the bank's deposit profile is concentrated. The top 20 depositors also remained concentrated at 19.27% of the total deposits as on March 31, 2018 compared to 21.41% as on March 31, 2017. Even though the bank's CASA ratio improved to 24.6% as on December 31, 2018 from 18.6% as on March 31, 2016, it remains below that of many other PVBs and the banking sector average. The increase in RBL's savings deposits resulted from the higher rates offered on the same, improved visibility through an increasing branch presence and branding efforts, and partly because of demonetisation. While the build-up in the savings accounts has been slower for the bank in the last two quarters, this was largely because of the management's focus on building the lower ticket savings accounts. With a high share of bulk deposits and surplus liquidity conditions, the cost of interest-bearing funds declined to 5.7% in FY2018 from 6.4% in FY2017 though it remained above the PVB average of 5.3% and 5.8%, respectively. However, with the tightening of liquidity, the cost of interest-bearing funds increased to 6.1% in 9M FY2019. Ability to further granulise the liability profile and maintain competitive cost of funds in tighter liquidity situations will be an important driver of sustained profitability.

Concentration of advances, albeit gradually reducing – RBL's top 20 group exposures accounted for 25% of the total exposures and 251% of the Tier I capital as on December 31, 2018 compared to 29% and 319%, respectively, as on March 31, 2016. The top 20 single borrower exposure accounted for 12.63% of the total exposures as on December 31, 2018 compared to 13.42% as on March 31, 2016. The concentration is gradually reducing, and the top borrower groups are higher-rated corporate groups, thereby providing some comfort. The bank's operations were initially concentrated in Maharashtra and North Karnataka. In the last six years, it has opened branches in other commercial zones like Delhi, Chennai and other metros. The expansion of the bank's footprint has resulted in lower geographic concentration. As on March 31, 2018, the western region accounted for 42% of net advances (38% in March 31, 2017), followed by 22% in the North (25%), 19% in the South (21%) and 17% in the East (16%).

Higher credit risk on unsecured portfolio – Following demonetisation, the bank's asset quality of microloans in the DB&FI segment suffered the most given the unsecured nature of lending and the marginal profile of the borrowers. The high delinquencies led to high credit provisioning for the bank in FY2018. RBL has provided entirely for the stressed portfolio till December 2018. Since its direct microfinance lending is sourced through BCs, it has first loss default guarantees (FLDG) of 3-5% on its microfinance book furnished by the BCs. This partly mitigates the loss. ~99.8% of the portfolio was generated post January 2017 and had a 90+dpd of ~0.33%. Further, the bank's agri portfolio (~3% of total advances as on December 31, 2018) was impacted by farm loan waivers. RBL has been increasing its exposure to credit cards (9% as on December 31, 2018), which are unsecured in nature (overall unsecured portfolio of 33% as on December 31, 2018) and expose the portfolio to credit risk. Over the medium term, RBL plans to increase its MFI portfolio to ~10% of its advances and the credit card portfolio to ~13-15% of its advances. Overall, these two unsecured segments are expected to account for ~23-25% of the loan portfolio over the medium term. RBL has managed these high-yielding loan portfolios with limited delinquencies (gross NPA of 0.9%, in MFI, and 1.1% in credit cards as on December 31, 2018). Ability to manage the asset quality while growing these product segments will be critical for RBL's profitability and solvency as the loss given on default in these segments is expected to be high.

Operating expenses remain high – Despite the strong growth in NII, improvement in NIMs and the increasing share of non-interest income, the bank's operating cost-to-income ratio[1] was high at 56.7% in FY2018 (57.3% in FY2017), surpassing the PVB average of 46.1% in FY2018 (operating expenses, as a percentage of ATA, stood at 2.7% for RBL compared to the PVB average of 2.2% for FY2018). While RBL's cost-income ratio improved to 52.6% in 9M FY2019, its operating expenses are expected to remain high with significant investments being made in infrastructure, branches and technology, in line with the scaling up of operations. Because of the high cost-income ratio, the bank's core operating profitability remains below the PVB averages. However, supported by the comfortable asset quality and controlled credit costs, the net profitability (PAT/ATA) is comparable to the PVB average.

Liquidity position

The bank's liquidity remains comfortable with 1-year negative structural liquidity gaps of 2.36% of outflows as on December 31, 2018. Its liquidity coverage ratio was comfortable at 119% as on December 31, 2018 against the regulatory requirement of 90% as on January 01, 2018 and 100% as on January 01, 2019. ICRA expects RBL to maintain comfortable liquidity given its access to call money markets and the RBI's repo and marginal standing facility mechanism in case of urgent liquidity needs.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA Rating Methodology for Banks
Parent / Group Support	Not applicable
Consolidation / Standalone	Standalone

About the company

Kolhapur, 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 with Mr Vishwavir Ahuja joining as the MD and CEO in June 2010. Following this, RBL's corporate office shifted to Mumbai. Apart from the management change, the bank underwent a change in shareholding in FY2011 with equity infusion from various private equity funds. From its erstwhile name of Ratnakar Bank Limited, the bank was rebranded to RBL Bank Limited in mid-2014. It was listed on the BSE and NSE with its IPO in August 2016. It is one of the fastest growing scheduled commercial banks in India with a presence in 16 states and Union Territories. As on December 31, 2018, RBL operated through 288 branches, 221 banking outlets, 956 BC branches (including banking outlets) and 390 ATMs.

[1] *Trading income is excluded from operating income for computing the operating cost-to-income ratio*

Key financial indicators (Audited)

	FY2017	FY2018	9M FY2018	9M FY2019
Net interest income	1,221	1,766	1,266	1,801
Profit before tax	681	967	696	939
Profit after tax	446	635	457	620
Net advances	29,449	40,268	36,890	49,893
Total assets	48,675	61,851	55,369	72,203
% CET 1	11.40%	13.61%	14.10%	12.50%
% Tier 1	11.40%	13.61%	14.10%	12.50%
% CRAR	13.72%	15.33%	15.90%	13.80%
% Net interest margin / Average total assets	2.78%	3.20%	3.24%	3.58%
% Net profit / Average total assets	1.02%	1.15%	1.17%	1.23%
% Return on net worth	13.46%	11.53%	11.27%	11.84%
% Gross NPAs	1.20%	1.40%	1.56%	1.38%
% Net NPAs	0.64%	0.78%	0.97%	0.72%
% Provision coverage excl. technical write-offs	46.77%	57.57%	52.54%	63.22%
% Net NPA/ Net worth	4.38%	4.68%	5.53%	4.92%

Amount in Rs. crore; All ratios are as per ICRA calculations
Source: Company, ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2019)					Chronology of Rating History for the Past 3 Years							
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Feb-19		FY2018		FY2017			FY2016	
						Aug-18	Jan-18	Oct-17	Mar-17	Dec-16	Jul-16	Feb-16	Jul-15
1	Certificate of Deposits	Short Term	6,000.00	NA	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[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+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+
3	Basel III Compliant Tier II Bond Programme	Long Term	800.00	730.00	[ICRA] AA- (hyb) (stable)	[ICRA] AA- (hyb) (stable)	[ICRA] AA- (hyb) (stable)	[ICRA]AA- (hyb) (stable)	[ICRA]A+ (hyb) (positive)	[ICRA] A+ (hyb) (stable)	[ICRA]A+ (hyb) (stable)	[ICRA]A+ (hyb) (stable); Assigned	NA
4	Medium-term Fixed Deposits	Medium Term	-	-	MAA (stable)	MAA (stable)	MAA (stable)	MAA (stable)	MAA- (positive)	MAA- (stable)	MAA- (stable)	MAA- (stable)	MAA- (stable)

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE976G08049	Basel III tier II bonds	16-Feb-16	10.25%	16-May-22	200.00	[ICRA]AA-(hyb) (stable)
INE976G08056	Basel III tier II bonds	31-Mar-16	10.25%	30-Jun-22	200.00	[ICRA]AA-(hyb) (stable)
INE976G08064	Basel III tier II bonds	27-Sep-16	10.20%	15-Apr-23	330.00	[ICRA]AA-(hyb) (stable)
NA	Basel III tier II bonds	Yet to be placed	-	-	70.00	[ICRA]AA-(hyb) (stable)
NA	Certificate of Deposits	-	-	7-365 days	6,000.00	[ICRA]A1+
NA	Short Term Fixed Deposits	NA	NA	NA	NA	[ICRA]A1+
NA	Medium Term Fixed Deposits	NA	NA	NA	NA	MAA (stable)

Source: RBL

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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