January 17, 2020

RBL Bank Limited: Ratings reaffirmed

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
Certificates of Deposit Programme	6,000.00	6,000.00	[ICRA]A1+; reaffirmed
Total	**6,800.00**	**6,800.00**	

The letters hyb, in parenthesis, suffixed to a rating symbol stand for hybrid, indicating that the rated instrument is a hybrid subordinated instrument with equity-like loss-absorption features; such features may translate into higher levels of rating transition and loss severity vis-à-vis conventional debt instruments. The rated Tier II bonds under Basel III are expected to absorb losses once the point of non-viability (PONV) trigger is invoked.

Rationale

The ratings reaffirmation factors in the recent capital raising by RBL Bank Limited (RBL), which is expected to provide a cushion on the capital levels amid the expected weakening in the asset quality in the corporate segment that could lead to elevated credit provisions and impact the net profitability over the near term. ICRA notes that though the bank's reported asset quality remains moderate, it is exposed to slippages from exposures to stressed groups that are currently classified as standard assets. The net non-performing advances (NNPAs) and the standard stressed group exposures declared by the bank (Rs. 1,000 crore) stood at 18.7% of its core equity capital[1] as on September 30, 2019 compared to 5.2% as on March 31, 2019. With the recent equity capital raising of Rs. 2,701 crore in December 2019 (4% of risk-weighted assets (RWAs) as on September 30, 2019), the bank is likely to be comfortably placed on its capital, solvency and growth requirements for the next 2 years.

The ratings continue to factor in the credit risks arising from RBL's increasing share of unsecured credit cards and microfinance loans, which accounted for 22% of the advances as on September 30, 2019 compared to 14% as on September 30, 2018. This is partially mitigated by the geographically diversified microloan portfolio and satisfactory and stable asset quality in the credit card segment, though the same remains a monitorable. In the corporate loan segment, the concentration of advances to the top 20 borrower groups, though on a declining trend, remained high at 19% of the total exposures and 249% of the Tier I capital as on June 30, 2019 (with the

[1] *Including capital of Rs. 2,701 crore, which was infused in December 2019*

recent capital infusion the top 20 borrower groups as a % of Tier 1 capital including capital infused would be lower at ~181%). ICRA takes note of the management's strategy to further reduce the concentration of the corporate exposures, given the recent stress witnessed in this segment.

The ratings continue to factor in the strong growth in retail liabilities and current and savings account (CASA) deposits. While RBL's CASA ratio has improved, it remains below that of many other private banks (PVBs) and the banking sector average, thereby translating into a higher cost of funds and the need to operate in high-yielding loan segments to generate adequate profitability. The bank's deposit profile is concentrated with the top 20 depositors accounting for 18.41% of the total deposits as on March 31, 2019 (19.27% as on March 31, 2018). Supported by the improving scale of operations and the focus on high-yielding assets like microfinance loans and the credit card business, RBL's operating profitability remains comparable with the PVB average despite the increase in the cost of funds and the higher operating expenses associated with the expansion of the new businesses and branch infrastructure.

Going forward, factoring in the slippages from the watchlist and other normal slippages, ICRA expects the solvency levels comfortable with net NPA/core equity well below the thresholds for negative rating trigger. With estimated credit growth of 15-25%, the bank is expected to maintain capital cushions of more than 3% over the regulatory Tier I level by March 2021. However, with an expected increase in the credit provisions, the return on assets (RoA) can weaken to ~0.6% in FY2020, depending on the extent of slippages and the provision cover maintained by the bank. This, however, is likely to improve in FY2021.

Key rating drivers and their description

Credit strengths

Demonstrated ability to raise capital; recent capital raise to support capitalisation and growth amid expected pressure on asset quality and profitability – RBL raised equity capital of Rs. 2,701 crore (35% of net worth and 4% of RWAs as on September 30, 2019) through a qualified institutional placement (QIP) and a preferential allotment in Q3 FY2020. Prior to this, it had raised capital through a preferential issue of Rs. 1,680 crore in August 2017 and Rs. 832 crore through an initial public offering (IPO) in August 2016. RBL reported Tier I and CRAR of 11.3% and 12.3% as on September 30, 2019 (12.5% and 13.7%, respectively, as on September 30, 2018). With increased delinquencies, the bank's net NPA/core equity increased to 12.1% as on September 30, 2019 (4.9% as on September 30, 2018). It has declared a standard exposure to stressed groups of Rs. 1,000 crore as on September 30, 2019, which could be a potential source of slippages in H2 FY2020. Under various scenarios of slippages from the watchlist apart from other slippages, ICRA expects the solvency levels comfortable with net NPA/core equity well below the thresholds for negative rating trigger. In ICRA's view, with the recent capital raise, the bank is comfortably placed to meet its capital requirements for the next two years despite the near-term pressure on internal capital generation.

Operating profitability supported by high-yielding advances but partially offset by high funding and operating costs – Despite interest reversals on slippages in H1 FY2020, the yield on advances increased to 11.8% in H1 FY2020 (10.7% in FY2019) with the change in the portfolio mix towards higher-yielding non-wholesale advances. The net interest margins (NIMs) improved to 4.0% of ATA in H1 FY2020 (3.6% in FY2019) with the increase in yields partially offset by the increase in the cost of interest-bearing funds (6.7% in H1 FY2020 compared to 6.1% in FY2019). The high NIMs and stable non-interest income (1.9% of ATA in H1 FY2020 and FY2019) translated into higher net operating income. While the operating income increased, RBL's operating expenses increased to 3.2% of ATA in H1 FY2020 (2.9% in FY2019), compared to the PVB average of 2.2%, thereby offsetting the benefits of higher NIMs.

RBL's cost-income ratio remains higher than its peers (54.5% in H1 FY2020 compared to 44.8% for PVBs) on account of the significant investments being made in infrastructure, branches and technology, in line with the scaling up of operations as well as the upfronting of credit card customer acquisition costs. The bank's branch network expanded to 346 as on September 30, 2019 from 268 as on September 30, 2018. ICRA expects the operating expenses to remain elevated as the bank is planning further branch expansion to 380-400 by March 31, 2020. Overall, the operating profitability stood at 2.7% of ATA in H1 FY2020 (2.6% in FY2019) compared to 2.8% for PVBs in H1 FY2020 and 2.6% in FY2019.

Steadily improving scale of operations; moderation in growth expected from past levels – The bank's loan book grew by 27% YoY to Rs. 58,476 crore as on September 30, 2019 with a QoQ growth of 3%. This was lower than RBL's medium-term plans of growing the loan book at a CAGR of 30-35% till FY2020. With the increased stress in the operating environment, the bank's wholesale advances grew at a slower pace of 13% YoY while the non-wholesale advances grew by a substantial 49% YoY. This is expected to slow down further in the next 1-2 years, given the increasing base, challenging operating environment and tightening of lending norms by the bank.

The growth in the non-wholesale advances was supported by retail assets (YoY growth of 49%) and micro banking (up 31% YoY), which was driven by the business correspondent (BC) branch expansion. Within retail assets, RBL witnessed strong growth in its credit cards portfolio (14% of the overall book on September 30, 2019). With slower growth in the corporate loan book, the share of wholesale advances reduced to 52% as on September 30, 2019 (59% as on September 30, 2018) and is expected to reduce further in the next 1-2 years.

Of the total portfolio, 64% was secured as on September 30, 2019 (68% as on September 30, 2018). 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 being higher than the sector average, the bank's market share in advances has been improving steadily and stood at 1.8% of PVB advances as on September 30, 2019 (1.6% in September 30, 2018).

Credit challenges

Delinquencies from stressed groups a key monitorable; internal capital generation to moderate in near term – With high slippages in Q2 FY2020 largely from corporate advances, the bank's asset quality weakened with the gross NPAs (GNPAs) increasing to 2.6% as on September 30, 2019 (1.4% as on both June 30, 2019 and September 30, 2018). The provision cover ratio (PCR) declined to 40.7% and the NNPAs rose to 1.56% as on September 30, 2019 (PCR of 47.4% and NNPA of 0.74% as on September 30, 2018). Despite the deterioration, the bank's gross and net NPAs were lower than the private banks' average of 4.3% and 1.7%, respectively, as on September 30, 2019.

The bank has, however, disclosed stressed exposure of ~Rs. 1,800 crore (including the vulnerable exposure of stressed groups) of which ~Rs. 800 crore became NPAs in Q2 FY2020. While RBL reported SMA1[2] and SMA2 of 0.45% and 0.39%, respectively, as on September 30, 2019, its asset quality is exposed to slippages from these standard exposures to stressed groups of Rs. 1,000 crore (~2% of advances and 13% of core equity as on September 30, 2019).

With a rise in slippages and a watchlist declared by RBL, the bank reported an increase in the credit provisions to 1.8% of ATA in H1 FY2020 from 0.9% in FY2019, resulting in a decline in the profit after tax (PAT)/ATA to 0.8% in H1 FY2020 compared to 1.2% in FY2019. ICRA expects the NIMs and operating profitability to largely remain stable in FY2020. However, with credit provisions expected to remain elevated at ~1.4-2.2% of ATA, the overall profitability is expected to moderate in the near term with ROA of ~0.6% in FY2020 depending on slippages and the PCR maintained by bank. This, however, is likely to improve in FY2021.

Resource profile remains concentrated; cost of funds higher than PVB average – The high growth in advances was supported by a YoY growth of 31% in the overall deposit base and a 42% increase in CASA deposits as on September 30, 2019. The bank's CASA ratio improved to 26.5% of total deposits as on September 30, 2019 from 24.5% as on September 30, 2018. The reliance on large ticket deposits remains high for the bank because of the high growth in the overall deposit base. RBL's deposit profile is concentrated. The top 20 depositors stood high at 18.41% of the total deposits as on March 31, 2019 compared to 19.27% as on March 31, 2018.

The bank witnessed a decline in the current account deposits in the last three quarters. However, the same was offset by the higher savings deposits with the management focusing on building the lower ticket granular savings accounts. RBL has witnessed an increase in its CASA ratio over the years (26.5% as on September 30, 2019 compared to 18.6% as on March 31, 2016), supported by the higher rates offered on savings deposits with improved visibility through an increasing branch presence. While the bank's CASA ratio has improved, it remains below that of many other PVBs and the banking sector average. RBL has been diversifying its liability profile by availing refinance under various programmes, such as USD 150 million by way of external commercial borrowings from IFC and refinance from SIDBI.

The cost of interest-bearing funds was higher than the PVB average and stood at 6.7% in H1 FY2020 and 6.1% in FY2019 compared to 5.7% and 5.4% for PVBs, respectively. The ability to granulise the liability profile and improve the cost of funds will be an important driver of the asset segments in which the bank operates and for sustained profitability.

High, albeit reducing, concentration of advances – RBL's top 20 group exposures accounted for 19% of the total exposures and 249% of the Tier I capital as on June 30, 2019 compared to 29% and 319%, respectively, as on March 31, 2016 (with the recent capital infusion the top 20 borrower groups as a % of Tier 1 capital including capital infused would be lower at ~181%). The top 20 single borrower exposures accounted for 11.41% of the total exposures as on March 31, 2019 compared to 13.42% as on March 31, 2016. While there has been some reduction

[2] *Special mention account (SMA) 1 is defined as a category in which stress, with respect to the principal and interest, has remained overdue for a period of more than 30 days and up to 60 days while SMA2 is one where it is overdue for more than 60 days and up to 90 days*

in the concentration, the same remains high. ICRA would monitor the management's plan of further reducing it going forward.

Increasing share on unsecured portfolio poses higher credit risk – The bank's unsecured portfolio increased to 36% as on September 30, 2019 from 32% as on September 30, 2018. The growth was largely due to by RBL's increased exposure to credit cards (14% of the overall book as on September 30, 2019 compared to 6% as on March 31, 2018), which are unsecured in nature and expose the portfolio to credit risk. Further, the bank has exposure of ~9% of overall book to microloans in the Development Banking & Financial Inclusion (DB&FI) segment. These two unsecured segments accounted for ~22% of the loan portfolio as on September 30, 209.

While RBL has managed these high-yielding loan portfolios with limited delinquencies (90+dpd of 0.9% in microloans and 1.8% in credit cards as on September 30, 2019), the portfolio is susceptible to asset quality pressure, given the unsecured nature of the loans and the marginal profile of the microloan borrowers. The bank had faced asset quality challenges in its microloan book post demonetisation. ICRA takes some comfort from the geographically diversified microloan portfolio with no state accounting for more than 15% of the portfolio and with ~50% of the portfolio covered through first loss default guarantee from the BCs who originate this portfolio. In the credit card segment, the bank has a tie-up with Bajaj Finance Limited [BFL; rated [ICRA]AAA(Stable)], whereby it sources the customers from the credit tested pool of BFL. The ability to manage the asset quality through economic cycles 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.

Liquidity position: Adequate

As per the structural liquidity statement, the bank has positive cumulative mismatches in the near-term buckets of up to 3 months, and negative cumulative mismatches of 3.1% and 1.6% of outflows in the 3-6 month and 6-month to 1-year buckets, respectively, as on November 30, 2019. Given the capital infusion in December 2019 and expectations of slower loan growth, the cumulative gaps across buckets could turn positive. On a fortnightly average basis, RBL has maintained excess SLR of ~6-7% of its net demand and time liabilities over the regulatory requirements during April-November 2019. Its liquidity coverage ratio was strong at 156% as on September 30, 2019, against the regulatory requirement of 100% as on January 01, 2019. However, given the high share of large ticket deposits, the ability to roll over these deposits will remain critical for sustaining liquidity. ICRA expects RBL to maintain adequate liquidity, given its access to call money markets, the RBI's repo and marginal standing facility mechanism and long term refinance in case of urgent liquidity needs.

Rating sensitivities

Positive triggers – ICRA could upgrade the ratings or revise the outlook to Positive if there is a sustained improvement in the granularity of the liability profile, with the share of CASA deposits exceeding 35% of the total deposits, accompanied with a decline in the cost of funds in relation to the sector. The bank's ability to improve the granularity of the loan book and maintain a strong asset quality and solvency profile while maintaining capital cushions of ~3% on Tier I over the regulatory levels and RoA of >1.25% on a sustained basis will be a key positive.

Negative triggers – 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 >25%

on a sustained basis. Further, sustained RoA < 1.0-1.1% and/or if the capital cushions over the regulatory levels fall below 3% at the Tier I levels on a sustained basis, will remain negative triggers. Moreover, a material weakening in the bank's liability franchise, impacting its resource profile, will also be a negative factor.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[ICRA Rating Methodology for Banks](#)
Parent/Group Support	Not applicable
Consolidation/Standalone	Standalone

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 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 renamed 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 September 30, 2019, RBL operated through 346 branches, 238 banking outlets, 1,156 BC branches (including banking outlets) and 394 ATMs.

Key financial indicators (audited)

	FY2018	FY2019	H1 FY2019	H1 FY2020
Net interest income	1,766	2,539	593	869
Profit before tax	967	1299	309	103
Profit after tax	635	867	205	54
Net advances	40,268	54,308	45,873	58,476
Total assets	61,851	80,359	67,206	87,678
% CET I	13.61%	12.10%	12.50%	11.30%
% Tier I	13.61%	12.10%	12.50%	11.30%
% CRAR	15.33%	13.46%	13.70%	12.30%
% Net interest margin / Average total assets	3.20%	3.57%	3.55%	4.01%
% Net profit / Average total assets	1.15%	1.22%	1.22%	0.76%
% Return on net worth	11.53%	12.18%	11.46%	8.38%
% Gross NPAs	1.40%	1.38%	1.40%	2.60%
% Net NPAs	0.78%	0.69%	0.74%	1.56%
% Provision coverage excl. technical write-offs	44.85%	50.60%	47.44%	40.73%
% Net NPA/ Core equity	4.78%	5.17%	4.85%	12.10%

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

Disclaimer: 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 of the instrument(s) mentioned herein.

Rating history for last three years

	Instrument	Type	Current Rating (FY2020)			Chronology of Rating History for the Past 3 Years						
			Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	17-Jan-20	FY2019		FY2018		FY2017		
						08-Feb-19	14-Aug-18	10-Jan-18	05-Oct-17	23-Mar-17	16-Dec-16	18-Jul-16
1	Certificates of Deposit	Short Term	6,000.00	NA	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ assigned	[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+
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]AA- (hyb) (stable); upgrade from [ICRA]A+ (hyb) (positive)	[ICRA]A+ (hyb) (positive); outlook revised to positive	[ICRA] A+ (hyb) (stable)	[ICRA]A+ (hyb) (stable)
4	Medium-term Fixed Deposits	Medium Term		-	MAA (stable)	MAA (stable)	MAA (stable)	MAA (stable)	MAA (stable); upgraded from MAA- (positive)	MAA- (positive); outlook revised to positive	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	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	Certificates of deposit	-	-	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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