August 25, 2022(Revised)

Bank of Baroda: Ratings reaffirmed; [ICRA]AA+ (Stable) assigned to Basel III Tier-I bonds

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Basel III Tier-I Bonds	-	2,500,00	[ICRA]AA+ (Stable); assigned
Basel III Tier-I Bonds	3,000.00	3,000.00	[ICRA]AA+ (Stable); reaffirmed
Basel III Tier II Bonds	2,450.00	2,450.00	[ICRA]AAA (Stable); reaffirmed
Infrastructure Bonds#	1,000.00	1,000.00	[ICRA]AAA (Stable); reaffirmed
Fixed Deposit Programme	-	-	[ICRA]AAA (Stable); reaffirmed
Total	**6,450.00**	**8,950.00**	

**Instrument details are provided in Annexure I; #Long-term bonds for financing infrastructure and affordable housing*

Rationale

The ratings factor in Bank of Baroda's (BoB) sovereign ownership, its strong franchise, and stable deposit base, which has led to a competitive cost of funds and superior liquidity. Moreover, BoB is the second largest public sector bank (PSB) in terms of advances and the fourth largest in the Indian financial system as on March 31, 2022. Given its importance, ICRA expects the bank to continue receiving support from the Government of India (GoI), if required. The ratings also consider the capital cushions that have improved in recent years, partly led by the capital raise via a qualified institutional placement (QIP) in FY2021 as well as the improvement in internal capital generation. While the enhanced profitability in FY2022 was supported by one-off reversals of provisions and recoveries on certain large corporate exposures, the overall profitability remains on an improving trajectory. Accordingly, ICRA expects the bank to remain self-sufficient for its capital requirements for absorbing incremental stress as well as for growth requirements while maintaining more than the desired cushion on the capital above the regulatory levels (including capital conservation buffers), driving the Stable outlook on the ratings.

The ratings take note of the monitorable book, comprising overdue and standard restructured advances, which has witnessed relatively higher slippages in recent quarters. Despite this, the overall headline asset quality metrics shall continue to improve. Given the high provision cover for the legacy stressed assets, ICRA expects that BoB's internal capital generation will continue to improve along with its asset quality and solvency position.

The rating for the Additional Tier – I (AT-I) bonds factors in the healthy level of distributable reserves (DRs) [1], which can be used to service the coupon on these bonds in a year of loss. As of June 30, 2022, the DR is estimated at 6.82% of the risk-weighted assets (RWAs).

Key rating drivers and their description

Credit strengths

Second largest PSB with majority sovereign ownership – The GoI remains the largest shareholder of BoB with a 63.97% equity stake as on June 30, 2022 and an aggregate infusion of Rs. 21,739 crore between FY2018 and FY2020 [including e-Dena Bank (e-DB) and e-Vijaya Bank (e-VB)]. BoB was the second largest PSB in the Indian banking sector as on March 31, 2022, in terms of advances with a 6.7% market share as well as a 6.5% share in the total deposits as on March 31, 2022.

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[1] Calculated as per the amendment in Basel III capital regulations for AT-I bonds by the RBI, vide its circular dated February 2, 2017. As per the amended definition, DRs include all reserves created through appropriations from the profit and loss account

Given its significance in the banking system, ICRA expects that BoB could be classified as a domestic systemically important bank (D-SIB). This means it could require additional equity capital over and above the minimum regulatory requirements, although this is not expected to be a challenge for the bank, given ICRA's outlook on the capital position. Further, ICRA expects BoB to receive support from the GoI in terms of capital as and when required, given its significant importance in the system.

Comfortable capital position while solvency profile improves – The bank's CET I and Tier I capital ratios were comfortable at 11.24% and 12.97%, respectively, as on June 30, 2022 despite the strong 19% year-on-year (YoY) growth in net advances to Rs. 8.0 lakh crore as on June 30, 2022. This was mainly due to the comparatively lower increase in the RWAs, which grew by 7% during the same period, as well as the improvement in internal capital generation. The bank raised equity of Rs. 4,500 crore from the market, which led to a reduction in the GoI's stake to 63.97% although the capital raise helped improve its capital cushions. In ICRA's view, BoB remains well placed in terms of its capital position for growth while absorbing any incremental stress and maintaining more than the desired cushion of 1% on the capital above the regulatory levels.

With the improved capital position as well as the decline in the net non-performing advances (NNPA) levels, the solvency[2] level improved to 18.2% as on March 31, 2022 from 33.4% as on March 31, 2021 and 39.0% as on March 31, 2020. Going forward, the solvency profile is expected to improve further even without any incremental capital raise. BoB infused capital, amounting to Rs. 300 crore in FY2023, into BoB Financial Services Limited {rated [ICRA]AAA (Stable)} to support the growth in its credit cards business, although the size of the capital support remains limited in relation to the bank's CET I level. Besides this, the subsidiaries largely remain self-sufficient in meeting their capital requirements in the near-to-medium-term and will require limited capital support from BoB.

Well-developed deposit franchise, leading to competitive cost of funds – Supported by its large branch network across India and well-developed customer franchise coupled with its widespread deposit franchise, the domestic current account and savings account (CASA) deposit base remained close to the PSB average. As it is the fourth largest public bank in terms of deposits, the CASA share remains strong for the bank with the CASA ratio at 41.50% of total deposits as on March 31, 2022. BoB operates with a low cost of interest-bearing funds, which stood at 3.51% in Q1 FY2023 (3.4% in FY2022 and 4.01% in FY2021), partially supported by the sizeable overseas asset and deposit base as well as the decline in the interest rates. Going forward, ICRA expects BoB's liability profile to remain a significant positive for supporting its credit growth while maintaining superior liquidity and profitability.

Earnings profile improves – The stronger growth in advances and the relatively lower interest reversals on fresh NPAs supported an improvement in the net interest margin (NIM) to 2.69% of average total assets (ATA) in FY2022 (2.50% in FY2021) and further to 2.77% in Q1 FY2023. Accordingly, the core operating profitability (before divestments and trading income) witnessed a steady improvement to 1.70% of ATA in FY2022 (1.49% in FY2021). Lower slippages in FY2022, in addition to recoveries as well as the reversal of proactive provisions on certain large corporate exposures, drove down the credit costs during FY2022-Q1 FY2023. As a result, credit costs moderated to 0.99% of ATA in FY2022 (1.27% in FY2021) and were even lower at 0.53% in Q1 FY2023.

While gains on the bond portfolios resulted in an improvement in the profit after tax to 0.60% of ATA in FY2022 (0.07% in FY2021), lower credit costs helped more than offset the impact of the losses on the bond portfolio in Q1 FY2023, with the return on assets improving to 0.68%. Going forward, ICRA expects that the credit costs shall remain at a moderate level because of the high provision cover on legacy stressed assets, which shall result in a continued improvement in the net profitability.

Credit challenges

Asset quality remains monitorable – Despite the adverse impact of the Covid-19 pandemic on borrowers, the annualised fresh NPA generation was contained at 2.08% in FY2022, which was lower compared to 2.99% in FY2022 and 3.72% in FY2020. This was also below the PSB average of 2.84% in FY2022. This was further supported by recoveries of Rs. 8,448 crore in FY2022 (Rs. 7,290 crore in FY2021). Write-offs remained elevated at Rs. 18,419 crore in FY2022 (Rs. 15,426 crore in FY2021). As a result,

[2] Solvency defined as (Net NPAs + Net security receipts + Net non-performing investments) / Core capital)

the headline asset quality metrics improved with the gross NPA (GNPA) and NNPA moderating to 6.26% and 1.58%, respectively, as on June 30, 2022 (8.85% and 3.03%, respectively, as on June 30, 2021).

As a part of the relief measures to borrowers impacted by Covid-19, BoB has restructured loans with a moratorium of up to two years for its borrowers. It had a standard restructured book of Rs. 19,666 crore (2.5% of standard advances) as on June 30, 2022. In addition, the special mention account (SMA)-1 and SMA-2 loan book (excluding ticket size of less than Rs. 5 crore) stood at 0.48% of standard advances on the aforementioned date. Till date, the overall slippage from the bank's restructured book is estimated at Rs. 4,000 crore, of which Rs. 1,000 crore was reported in Q1 FY2023. This led to an uptick in the fresh NPA generation rate to 2.28% in Q1 FY2023. While ICRA expects that the overall slippages should incrementally tend to be lower compared to the last few years, leading to a steady reduction in the credit cost, the asset quality will remain a monitorable for these advances.

Liquidity position: Superior

BoB's liquidity profile remains superior supported by a high statutory liquidity ratio (SLR) of 21.93% of the net demand and time liabilities (NDTL) as on March 31, 2022 (above the regulatory requirement of 18%). ICRA expects BoB to maintain superior liquidity, given the large proportion of retail deposits and the high portfolio of liquid investments. It can also avail liquidity support from the Reserve Bank of India (RBI; through reverse repo against excess SLR investments and the marginal standing facility mechanism) in case of urgent requirement.

Rating sensitivities

Positive factors – Not applicable as all the ratings are at the highest possible level

Negative factors – Given its sovereign ownership and its position as the second largest PSB, ICRA expects BoB to receive the requisite capital support from the GoI, if required. Any dilution in the expected stance will be a credit negative. Solvency weaker than 40% on a sustained basis could also be a credit negative for the bank.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA Rating Methodology for Banks Impact of Parent or Group Support on an Issuer's Credit Rating Rating approach – Consolidation
Parent/Group support	The ratings factor in BoB's sovereign ownership and the demonstrated track record of capital infusion by the GoI. ICRA expects the GoI to support BoB with capital infusions, if required.
Consolidation/Standalone	The ratings are based on the standalone financial statements of BoB. However, in line with ICRA's limited consolidation approach, the capital requirements of BoB's key subsidiaries have been factored in while assessing its credit profile.

About the company

Bank of Baroda was incorporated in 1908 and nationalised in 1969, along with 13 other major commercial banks of India, by the GoI. BoB is headquartered in Vadodara while its corporate office is in Mumbai.

On September 17, 2018, the GoI announced the merger of Vijaya Bank and Dena Bank with BoB. The merger came into effect on April 01, 2019. As of March 31, 2022, BoB had 8,168 branches and 10,033 ATMs across India, of which ~60% are rural/semi-urban branches. It has an international presence spanning 94 overseas offices across 17 countries. Post-merger, BoB became the fourth largest PSB in the Indian banking sector in terms of total business (advances and deposits cumulatively as on June 30, 2022). The GoI held a 63.97% stake in the bank as on June 30, 2022.

BoB reported a net profit of Rs. 2,168 crore in Q1 FY2023 on a total asset book of Rs. 12.85 lakh crore[3]. Its GNPA and NNPA stood at 6.26% and 1.58%, respectively, as on June 30, 2022. The regulatory capital adequacy ratio stood at 15.46% as on June 30, 2022 (CET I: 11.24% and Tier I of 12.97%).

Key financial indicators (standalone)

	FY2021	FY2022	Q1 FY2022	Q1 FY2023
Net interest income	28,809	32,621	7,892	8,838
Profit before tax	5,556	9,386	1,596	2,843
Profit after tax	829	7,272	1,209	2,168
Net advances (Rs. lakh crore)	7.06	7.77	6.69	7.99
Total assets* (Rs. lakh crore)	11.50	12.71	11.16	12.85
Net interest margin / Average total assets	2.50%	2.69%	2.79%	2.77%
Return on assets	0.07%	0.60%	0.43%	0.68%
Return on net worth	1.15%	9.23%	6.67%	10.02%
CET I	10.94%	11.42%	11.25%	11.24%
Tier I	12.67%	13.18%	13.06%	12.97%
CRAR	14.99%	15.68%	15.4%	15.46%
Gross NPA	8.87%	6.61%	8.85%	6.26%
Net NPA	3.09%	1.72%	3.03%	1.58%
PCR (excl TWO)	67%	75%	67.86%	75.94%
Solvency	33.4%	18.22%	31.34%	18.55%

Source: BoB, ICRA Research; Amount in Rs. crore unless mentioned otherwise
** Excluding revaluation reserve; All ratios as per ICRA's calculations*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

[3] *Excluding revaluation reserves*

Rating history for past three years

Sr. No.	Name of Instrument	Current Rating (FY2023)						Chronology of Rating History for the Past 3 Years			
		Type	Rated Amount (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2023			Date & Rating in FY2022		Date & Rating in FY2021	Date & Rating in FY2020
					Aug-25-2022	Aug-05-2022	Jun-01-2022	Nov-17-2021	Jun-30-2021	Jun-12-2020	Apr-26-2019
1	Basel III Tier II Bonds	Long Term	1,000.0	1,000.0	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA(hyb) (Stable)	[ICRA]AAA(hyb) (Stable)	[ICRA]AAA(hyb) (Stable)
2	Fixed Deposit Programme	Long Term	NA	NA	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	MAAA (Stable)	MAAA (Stable)	MAAA (Stable)	MAAA (Stable)
3	Basel III Tier II Bonds	Long Term	1,450.0	1,450.0	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA(hyb) (Stable)	[ICRA]AAA (hyb) (Stable)	[ICRA]AAA(hyb) (Stable)
4	Basel III Tier-I Bonds	Long Term	325.0	0.00	-	[ICRA]AA+ (Stable); Withdrawn	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+(hyb) (Stable)	[ICRA]AA(hyb) (Stable)	[ICRA]AA(hyb) (Stable)
5	Basel III Tier-I Bonds	Long Term	3,000.0	2,749.0	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	-	-	-
6	Infrastructure Bonds	Long Term	1,000	1,000	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-	-	-	-
7	Basel III Tier-I Bonds	Long Term	2,500	Yet to be placed	[ICRA]AA+ (Stable) Assigned	-	-	-	-	-	-

Source: ICRA Research

Complexity level of the rated instrument

Instrument	Complexity Indicator
Basel III Tier II Bonds	Highly Complex
Basel III Tier-I Bonds	Highly Complex
Fixed Deposit	Very Simple
Infrastructure Bonds	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 instruments 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	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE705A08037	Tier II Bonds – Basel III	Oct-30-2014	9.15%	Oct-30-2024	500.00	[ICRA]AAA (Stable)
INE705A08052	Tier II Bonds – Basel III	Feb-18-2015	8.62%	Feb-18-2025	500.00	
INE705A08078	Tier II Bonds – Basel III	Jan-22-2016	8.64%	Jan-22-2026	450.00	
INE028A08059	Tier II Bonds – Basel III	Dec-17-2013	9.73%	Dec-17-2023	1,000.00	
INE028A08265	AT-I Bonds – Basel III	Nov-26-2021	7.95%	Nov-26-2026^	1,997.00	[ICRA]AA+ (Stable)
INE028A08273	AT-I Bonds – Basel III	Jan-31-2022	8.00%	Jan-31-2027^	752.00	[ICRA]AA+ (Stable)
Yet to be issued	AT-I Bonds – Basel III	-	-	-	251	[ICRA]AA+ (Stable)
INE028A08281	Infrastructure Bonds	Aug-17-2022	7.39%	Aug-17-2029	1,000	[ICRA]AAA (Stable)
Yet to be issued	AT-I Bonds – Basel III	-	-	-	2,500	[ICRA]AA+ (Stable)
NA	Fixed Deposits	-	-	-	-	[ICRA]AAA (Stable)

^First call option date; first call option after five years from issuance date
Source: BoB

Key features of the rated instruments
The servicing of the Basel III Tier II bonds is not subject to any capital ratios and profitability. However, these bonds are expected to absorb losses once the point of non-viability (PONV) trigger is invoked.

The rated Basel III Tier-I Bonds (AT-I bonds) have the following loss-absorption features that make them riskier:

- Coupon payments are non-cumulative and discretionary, and the bank has full discretion at all times to cancel coupon payments. Cancellation of discretionary payments shall not be an event of default.
- Coupons can be paid out of the current year's profits. However, if the current year's profit is not sufficient or if the payment of the coupon is likely to result in a loss, the coupon payment can be made through the reserves and surpluses created through the appropriation of profits (including statutory reserves). The coupon payment is subject to the bank meeting the minimum regulatory requirements for CET I, Tier I and total capital ratios (including capital conservation buffer; CCB) at all times as prescribed by the RBI under the Basel III regulations.

These Tier-I bonds are expected to absorb losses through the write-down mechanism at the objective prespecified trigger point fixed at the bank's CET I ratio as prescribed by the RBI, i.e. 6.125% of the total RWAs of the bank, or when the PONV trigger is breached in the RBI's opinion.

Given the above distinguishing features of the AT-I bonds, ICRA has assigned a one notch lower rating to these than the rating on the Tier II instruments. The DRs that can be used for servicing the coupon in a situation of inadequate profit or a loss during the year stood at a comfortable 6.82% of RWAs as on June 30, 2022. The rating on the Tier-I bonds continues to be supported by the bank's capital profile (CET I: 11.24%, Tier I: 12.97% and CRAR: 15.46% as on June 30, 2022), which is likely to remain comfortable, given the outlook on BoB's profitability and its healthy capital-raising ability.

Annexure II: List of entities considered for consolidated analysis

S. No.	Name of the entity	Ownership	Consolidation Approach
1	**BOB Financial Solutions Limited**	100.00%	Limited Consolidation
2	**BOB Capital Markets Limited**	100.00%	Limited Consolidation
3	**Baroda Global Shared Services Limited**	100.00%	Limited Consolidation
4	**Baroda Sun Technologies Limited**	100.00%	Limited Consolidation
5	**Baroda Asset Management India Limited**	100.00%	Limited Consolidation
6	**Baroda Trustee India Private Limited**	100.00%	Limited Consolidation
7	**Bank of Baroda (Botswana) Limited**	100.00%	Limited Consolidation
8	**Bank of Baroda (Guyana) Limited**	100.00%	Limited Consolidation
9	**Bank of Baroda (New Zealand) Limited**	100.00%	Limited Consolidation

10	**Bank of Baroda (Tanzania) Limited**	100.00%	Limited Consolidation
11	**Bank of Baroda (UK) Limited**	100.00%	Limited Consolidation
12	**Nainital Bank**	98.57%	Limited Consolidation
13	**Bank of Baroda (Kenya) Limited**	86.70%	Limited Consolidation
14	**Bank of Baroda (Uganda) Limited**	80.00%	Limited Consolidation
15	**India First Life Insurance Company Limited**	44.00%	Limited Consolidation
16	**India Infradebt Limited**	40.99%	Limited Consolidation
17	**India International Bank (Malaysia), Berhad**	40.00%	Limited Consolidation
18	**Baroda Uttar Pradesh Gramin Bank**	35.00%	Limited Consolidation
19	**Baroda Rajasthan Gramin Bank**	35.00%	Limited Consolidation
20	**Baroda Gujarat Gramin Bank**	35.00%	Limited Consolidation
21	**Indo-Zambia Bank Limited**	20.00%	Limited Consolidation

Source: BoB

Corrigendum

Rationale dated August 25, 2022, has been revised with changes as below:

Addition of "Rating Approach- Consolidation" in the analytical approach section

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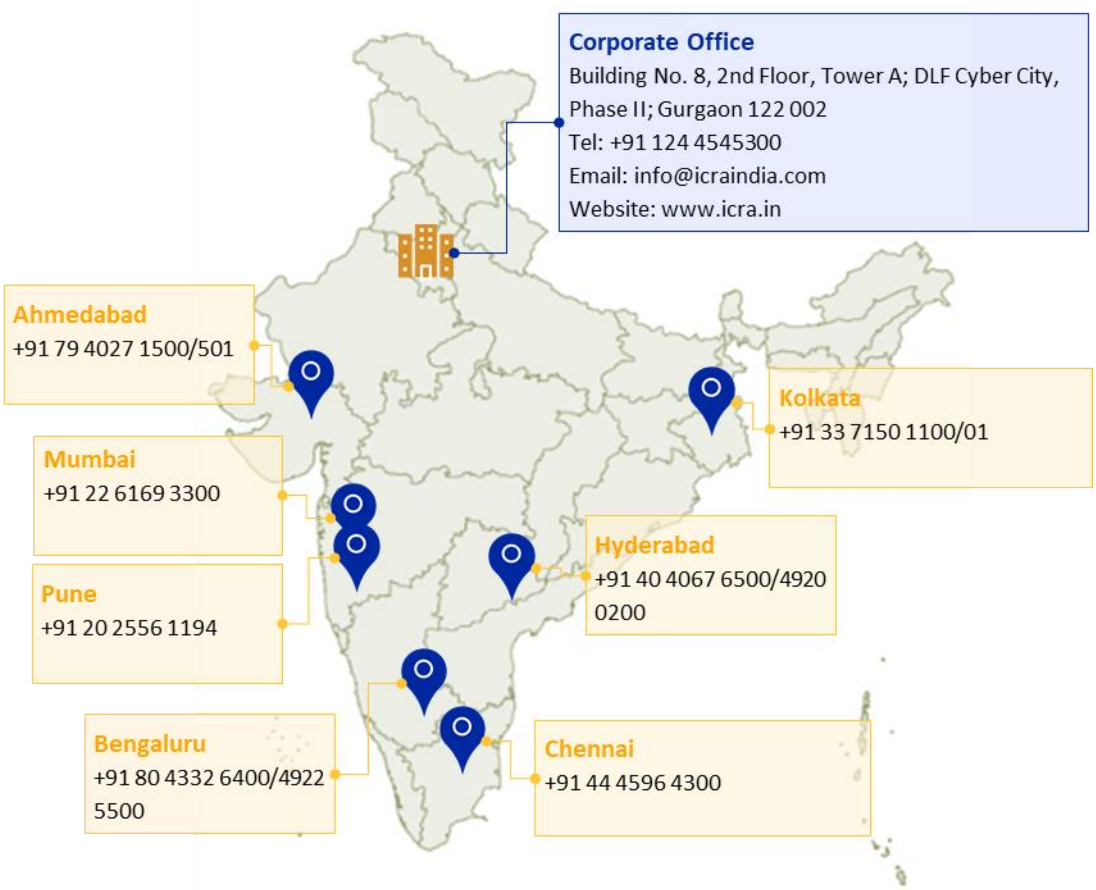

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