August 11, 2023

Bank of Baroda: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Basel III Tier-I Bonds	5,500.00	5,500.00	[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	**8,950.00**	**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, translating in a steady deposit growth, while maintaining 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, 2023. The ratings factor in the improvement in BoB's profitability and solvency profile, which is expected to be maintained going forward, while the overall capitalisation profile remains comfortable. 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; CCB), driving the Stable outlook on the ratings.

While the headline asset quality indicators have improved, the ratings take note of the residual vulnerable book, comprising overdue (SMA[1]-1, SMA-2) and standard restructured advances, although it has witnessed a sustained moderation from the comparatively higher levels a year back. Given the high provision cover for the legacy stressed assets, ICRA expects that BoB's internal capital generation will continue to be strong along with its asset quality and solvency position. The rating for the Tier-I (AT-I) bonds factors in the healthy level of distributable reserves (DRs), which can be used to service the coupon on these bonds in the unforeseeable event of a loss.

The Stable outlook on the ratings factors in the expectation of an improvement in the solvency profile and internal capital generation and the strong liability profile, apart from the bank's sovereign ownership.

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, 2023 and an aggregate equity infusion of Rs. 21,739 crore between FY2018 and FY2020 [including e-Dena Bank (e-DB) and e-Vijaya Bank (e-VB)] reflects GoI's support. BoB is the second largest PSB in the Indian banking sector as on March 31, 2023, in terms of advances with a 7.0% market share as well as a 6.7% share in the total deposits as on March 31, 2023. 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 11.94% and 13.64%, respectively, as on June 30, 2023 despite the strong 20% year-on-year (YoY) growth in net advances to

[1] *SMA is defined as a special mention account (SMA), which is an account exhibiting signs of incipient stress resulting in the borrower defaulting in the timely servicing of their debt obligations though the account has not yet been classified as an NPA as per the extant RBI guidelines; SMA-1 accounts are overdue by 31-60 days while SMA-2 accounts are overdue by 61-90 days*

Rs. 9.6 lakh crore as on June 30, 2023. This was mainly due to the comparatively lower increase in the risk-weighted assets (RWAs), which grew by 12% during the same period, as well as the improvement in internal capital generation. 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) level, the solvency[2] level improved to 10.5% as on March 31, 2023 from 19.1% as on March 31, 2022. Going forward, the solvency profile is expected to improve further even without any incremental capital raise. BoB also infused capital, amounting to Rs. 700 crore in FY2023, into BoB Financial Solutions 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.

Notwithstanding the improvement in the capitalisation profile, the RBI recently issued a discussion paper for transitioning to the expected loss framework for credit exposures. As highlighted by ICRA, banks with a high share of overdue/restructured loans could see a one-time impact on their capital position upon transitioning. While the RBI has proposed these provisions to be spread over a five-year period for the computation of the regulatory capital ratios, the impact on the capital position (without taking regulatory forbearance) will remain a monitorable.

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 bank's domestic current account and savings account (CASA) deposit base remained close to the PSB average. As it is the second largest PSB in terms of deposits, BoB's CASA share remains strong with the CASA ratio at ~35% of total deposits as on June 30, 2023. BoB operates with a low cost of interest-bearing funds, which stood at 4.75% in Q1 FY2024 (3.9% in FY2023 and 3.4% in FY2022). 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 the improvement in the net interest margin (NIM) to 3.04% in FY2023 (2.69% in FY2022), although as the cost of funds steadily rose, NIMs witnessed a mild moderation to 3.01% of average total assets (ATA) in Q1 FY2024. Nonetheless, the core operating profitability (before divestments and trading income) witnessed a steady improvement to 2.05% of ATA in Q1FY2024 (1.97% in FY2023, 1.70% in FY2022). Lower slippages, in addition to recoveries as well as the reversal of proactive provisions on certain large corporate exposures, drove down the credit costs in recent years. As a result, annualised credit costs moderated and stood at 0.36% in FY2023 from 0.99% in FY2022, although it rose slightly to 0.53% in Q1 FY2024. 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 lower treasury gains in FY2023, with the return on assets strengthening to 1.04% in FY2023 and further to 1.12% (annualised) in Q1 FY2024. 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 support net profitability.

Credit challenges

Asset quality remains monitorable – The overall gross fresh NPA generation eased to 1.2% (annualised) in Q1FY2024 (1.5% in FY2023, 2.1% in FY2022) and was materially lower than the elevated levels seen in the past (~3-7% during FY2016-FY2020). Healthy recoveries, elevated write-offs (Rs. 18,347 crore in FY2023 and Rs. 18,419 crore in FY2022) and upgrades also supported the headline asset quality metrics with the gross NPA (GNPA) and NNPA moderating to 3.51% and 0.78%, respectively, as on June 30, 2023 (6.26% and 1.58%, respectively, as on June 30, 2022). Moreover, the share of the vulnerable book in relation to the total standard assets and the core capital has continued to moderation, although the performance of the residual vulnerable book (~1.8% of standard advances) as well as the bank's ability to limit slippages will remain a near-to-

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

medium-term monitorable. Further the impact of the weakening macro-economic factors could also affect the debt-servicing ability of borrowers and remains a monitorable.

Environmental and social risks

While banks like BoB 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 risk is not material for BoB 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. BoB has not faced material lapses over the years. Customer preferences are increasingly shifting towards digital banking, which provides an opportunity to reduce the operating costs. BoB has been making the requisite investments to enhance its digital interface with its customers. While it contributes to promoting financial inclusion by lending to the underserved segments, its lending practices remain prudent as reflected in the healthy asset quality numbers in this segment compared with its peers.

Liquidity position: Superior

BoB's liquidity profile remains superior supported by a high statutory liquidity ratio (SLR) of 22.26% of the net demand and time liabilities (NDTL) as on June 16, 2023 (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 level for the respective instruments

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[1] weaker than 40% on a sustained basis could also be a credit negative for the bank. A sharp deterioration in the profitability, leading to a weakening in the DRs eligible for the coupon payment on the AT-I bonds, will be a negative trigger for the rating on these bonds.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA Rating Methodology for Banks and Financial Institutions Impact of Parent or Group Support on an Issuer's Credit Rating ICRA's Rating Methodology on Consolidation.
Parent/Group support	The ratings factor in BoB's sovereign ownership and the demonstrated track record of capital infusions 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 became effective on April 01, 2019. As of March 31, 2023, BoB had 8,200 branches and 9,764 ATMs across India, of which ~60% are rural/semi-urban branches. It has an international presence with 93 overseas offices in 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, 2023). The GoI held a 63.97% stake in the bank as on June 30, 2023.

BoB reported a net profit of Rs. 4,070 crore in Q1 FY2024 on a total asset book of Rs. 14.67 lakh crore[3]. Its GNPA and NNPA stood at 3.51% and 0.78%, respectively, as on June 30, 2023. The regulatory capital adequacy ratio stood at 15.84% as on June 30, 2023 (CET I: 11.94% and Tier I of 13.64%).

Key financial indicators (standalone)

	FY2022	FY2023	Q1 FY2023	Q1 FY2024
Net interest income	32,621	41,356	8,838	10,997
Profit before tax	9,386	19,727	2,843	5,878
Profit after tax	7,272	14,110	2,168	4,070
Net advances (Rs. lakh crore)	7.77	9.41	7.99	9.63
Total assets* (Rs. lakh crore)	12.71	14.53	12.85	14.67
Net interest margin / Average total assets	2.69%	3.04%	2.77%	3.01%
Return on assets	0.60%	1.04%	0.68%	1.12%
Return on net worth	9.23%	15.28%	10.37%	17.25%
CET I	11.42%	12.24%	11.24%	11.94%
Tier I	13.18%	13.99%	12.97%	13.64%
CRAR	15.68%	16.24%	15.46%	15.84%
Gross NPA	6.61%	3.79%	6.26%	3.51%
Net NPA	1.72%	0.89%	1.58%	0.78%
PCR (excl. TWO)	75%	77%	76%	79%
Solvency (NNPA/CET)	18.22%	9.82%	17.61%	8.73%

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 (FY2024)				Chronology of Rating History for the Past 3 Years						
		Type	Rated Amount (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023			Date & Rating in FY2022		Date & Rating in FY2021
					Aug-11-2023	Aug-25-2022	Aug-05-2022	Jun-01-2022	Nov-17-2021	Jun-30-2021	Jun-12-2020
1	**Basel III Tier II Bonds**	Long Term	1,000.00	1,000.00	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (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)**	**[ICRA]AAA (Stable)**	**MAAA (Stable)**	**MAAA (Stable)**	**MAAA (Stable)**
3	**Basel III Tier II Bonds**	Long Term	1,450.00	1,450.00	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA(hyb) (Stable)**	**[ICRA]AAA(hyb) (Stable)**
4	**Basel III Tier-I Bonds**	Long Term	-	-	-	-	-	-	-	**[ICRA]AA+(hyb) (Stable)**	**[ICRA]AA(hyb) (Stable)**
5	**Basel III Tier-I Bonds**	Long Term	-	-	-	-	**[ICRA]AA+ (Stable);**	**[ICRA]AA+ (Stable)**	**[ICRA]AA+ (Stable)**	**[ICRA]AA+(hyb) (Stable)**	**[ICRA]AA(hyb) (Stable)**
6	**Basel III Tier-I Bonds**	Long Term	3,000.00	2,749.00^	**[ICRA]AA+ (Stable)**	**[ICRA]AA+ (Stable)**	**[ICRA]AA+ (Stable)**	**[ICRA]AA+ (Stable)**	**[ICRA]AA+ (Stable)**	-	-
7	**Infrastructure Bonds**	Long Term	1,000.00	1,000.00	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	**[ICRA]AAA (Stable)**	-	-	-	-
8	**Basel III Tier-I Bonds**	Long Term	2,500.00	2,474.00^	**[ICRA]AA+ (Stable)**	**[ICRA]AA+ (Stable)**	-	-	-	-	-

Source: ICRA Research; ^ Balance yet to be issued; 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 Bonds	Highly Complex
Basel III Tier-I Bonds	Highly Complex
Fixed Deposits	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 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	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)
INE028A08281	**Infrastructure Bonds**	Aug-17-2022	7.39%	Aug-17-2029	1,000.00	[ICRA]AAA (Stable)
INE028A08299	**AT-I Bonds – Basel III**	Sep-02-2022	7.88%	Sep-02-2027^	2,474.00	[ICRA]AA+ (Stable)
Yet to be issued	**AT-I Bonds – Basel III**	-	-	-	277.00	[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, the Basel III Tier II bonds and Basel III Tier-I bonds (AT-I bonds) are expected to absorb losses once the point of non-viability (PONV) trigger is invoked.

Further, the exercise of the call option on the Basel III Tier-II and Tier-I bonds is contingent upon the prior approval of the RBI. Moreover, the bank will need to demonstrate that the capital position is well above the minimum regulatory requirement, post the exercise of the said call option.

The rated Tier-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. 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[4] created via the appropriation of profits (including statutory reserves). However, the coupon payment is subject to the bank meeting the minimum regulatory requirements for CET I, Tier I and total capital ratios (including 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 Tier I bonds, ICRA has assigned a one notch lower rating to these than the rating for 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 6.68% of RWAs as on March 31, 2023.

The rating on the Tier I bonds continues to be supported by the bank's capital profile, which is likely to remain comfortable, given the outlook on BoB's profitability. However, the transition to the expected credit loss (ECL) framework and its impact on the capital and DRs remain monitorable.

[4] *Calculated as per the amendment in Basel III capital regulations for Tier-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*

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	**Bank of Baroda (Botswana) Limited**	100.00%	Limited Consolidation
6	**Bank of Baroda (Guyana) Inc.**	100.00%	Limited Consolidation
7	**Bank of Baroda (New Zealand) Limited**	100.00%	Limited Consolidation
8	**Bank of Baroda (Tanzania) Limited**	100.00%	Limited Consolidation
9	**Bank of Baroda (UK) Limited**	100.00%	Limited Consolidation
10	**The Nainital Bank Ltd**	98.57%	Limited Consolidation
11	**Bank of Baroda (Kenya) Limited**	86.70%	Limited Consolidation
12	**Bank of Baroda (Uganda) Limited**	80.00%	Limited Consolidation
13	**IndiaFirst Life Insurance Company Limited**	65.00%	Limited Consolidation
14	**Baroda BNP Paribas Asset Management India Ltd**	50.10%	Limited Consolidation
15	**Baroda BNP Paribas Trustee India Private Limited**	50.10%	Limited Consolidation
16	**India Infradebt Limited**	40.99%	Limited Consolidation
17	**India International Bank (Malaysia), Berhad**	40.00%	Limited Consolidation
18	**Baroda U P Bank**	35.00%	Limited Consolidation
19	**Baroda Rajasthan Kshetriya 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; Stake as on March 31, 2023

ANALYST CONTACTS

Karthik Srinivasan
+91 22 6114 3444
karthiks@icraindia.com

Anil Gupta
+91 124 4545 314
anilg@icraindia.com

Aashay Choksey
+91 22 6114 3430
aashay.choksey@icraindia.com

Sohil Mehta
+91 22 6114 3449
sohil.mehta@icraindia.com

Vaibhav Arora
+91 124 4545 386
vaibhav.arora@icraindia.com

RELATIONSHIP CONTACT

Mr. L. Shivakumar
+91 22 6114 3304
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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.

For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches