November 23, 2017

DCB Bank Limited

Summary of rated instruments

Instrument*	Rated Amount (Rs. crore)	Rating Action
Basel III Compliant Tier II Bonds Programme	550.00	[ICRA]A+(hyb)(stable); reaffirmed
Short Term Fixed Deposit Programme	-	[ICRA]A1+; reaffirmed
Total	**550.00**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the rating of [ICRA]A+(hyb)(stable) (pronounced ICRA A plus hybrid with a stable outlook) to the Rs. 550 crore Basel III compliant Tier II bonds programme and the rating of [ICRA]A1+ (pronounced ICRA A one plus) to the Short Term Fixed Deposit Programme of DCB Bank Limited (DCB)[1]. 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 are expected to absorb losses once the "Point of Non Viability" (PONV) trigger is invoked.

Rationale

The ratings factor in the healthy and consistent growth in advances of the bank, its comfortable asset quality given its focus on the relatively safer mortgage segment, its low exposure to vulnerable sectors, its stable top management, and its adequate capitalisation levels following the Rs. 379 crore equity raise via qualified institutional placement which would support future growth of bank. The ratings also factor in the improving net interest margins (NIMs) albeit with moderate profitability in light of branch expansion drive undertaken by the bank. The ratings remain constrained by banks elevated cost to income ratio and its low but improving CASA deposits. ICRA takes note of the weakening in asset quality in the mortgage and Agri and Inclusive banking (AIB) segment due to the impact of events including demonetization, implementation of Goods and Service Tax (GST), enforcement of Bharat Stage IV emission norms and the implementation of Real Estate (Regulation and Development) Act (RERA) which has led to some disruptions in the market. ICRA will monitor the trends in the bank's asset quality post the ongoing transitory period.

Going forward, the bank's ability to maintain its net interest margins in light of competition from small finance banks, its ability to improve its CASA ratio and thus its cost of deposits while maintaining sound asset quality will be the key rating sensitivities.

[1] For complete rating scale and definitions, please refer to ICRA's website (www.icra.in) or other ICRA rating publications.

Key rating drivers

Credit strengths

- **Steady growth in loan book** – DCB has grown its advances at a healthy pace of 24% CAGR over the 5 years spanning FY2012 – FY2017 which is higher than the industry average, albeit on a modest loan book size. During FY2017, DCB grew its net advances by 22% to Rs. 15,818 crore as on March 31, 2017 as compared to Rs. 12,921 crore as on March 31, 2016 which is higher as compared to the growth rate of 4% for the banking industry and a growth rate of 15% for private banks. The portfolio further grew to Rs. 17,395 crore as on September 30, 2017. Growth for DCB has been driven by the mortgage, Agri and Inclusive banking (AIB), corporate banking and SME/MSME segments which constituted 42%, 17%, 17% and 12% respectively of net advances as on September 30, 2017. The share of AIB segment has been on an upward trend due to its higher growth vis-a-vis the overall portfolio. The bank's advances are well-diversified with a relatively low exposure to sensitive sectors such as infrastructure (including energy, telecommunication, water & sanitation and social and commercial infrastructure), construction and commercial real estate. The bank will look to double its balance sheet over the next 3 to 3½ year period, translating to a targeted book growth of 22-24% YoY.
- **Comfortable asset quality** –The bank's asset quality remained comfortable with gross and net NPAs of 1.80% and 0.90% respectively as on September 30, 2017 (1.59% and 0.79% as on March 31, 2017 and 1.51% and 0.75% as on March 31, 2016). The slippages for the bank increased in H1FY2018 contributed primarily by the mortgage and AIB segments. The bank's standard restructured assets remained low at 0.4% of the total advances as on March 31, 2017 with SDR accounts of 0.9%. The bank does not have any CDR, S4A or 5/25 refinancing accounts. DCB's security receipts stood at 0.4% as on September 30, 2017. Also, the bank's exposure to accounts identified by RBI for insolvency proceedings remains low. While provision coverage ratio for the bank declined to 71.96% as on September 30, 2017 from 73.80% as on March 31, 2017 it remains higher than the industry average of 61% for private banks. Overall, despite the weakening, the bank's asset quality remains comfortable.
- **Adequate capitalisation levels for proposed growth plans –** The bank's capital ratios (Tier 1 and CRAR as % of risk weighted assets) stood at 12.90% and 14.65% respectively as on September 30, 2017 (11.87% and 1.89% respectively as on March 31, 2017), which were higher than the regulatory levels. The solvency remained strong with net NPAs/net worth of 6.4% as on September 30, 2017 (6.4% as on March 31, 2017 and 5.6% as on March 31, 2016), and was better than industry average. The bank raised Rs. 379 crore in May 2017, by way of qualified institutional placement (QIP) resulting into an improvement in the capitalisation. With the capital infusion, the bank is adequately capitalised to meet its medium term growth targets.
- **Healthy interest margins** – The net interest margins (NIMs) for DCB have been on an upward trend supported by a healthy CASA growth. NIMs were reported at a healthy 4.22% during H1FY2017 as compared to 4.04% during FY2017 and 3.94% during FY2016 which is higher as compared to the industry average and the average for private sector banks. With the bank migrating to the MCLR regime effective April 1, 2017 the NIMs are expected to moderate in the near term however they are expected to remain at healthy levels. Going forward, the ability of the bank to protect its yields in light of competition from small finance banks, its ability to grow its CASA supported by its improved branch network and its ability to maintain stable asset quality indicators would have an impact on the interest margins and would thus be a monitorable.

Credit weaknesses

- **Concentrated resource profile; albeit improving–**While the CASA deposits for the bank improved to 26% as on September 30, 2017 from 23% as on March 31, 2016 supported by both demonetisation and the increased branch presence, the ratio remains lower as compared to many other private sector banks. The share of deposits over Rs. 1 crore remained high at 28% as on September 30, 2017 (as compared to 27% as on March 31, 2016).With the bank doubling its branch network in two years to 306 as on September 30, 2017 from 160 as on September 30, 2015, ICRA expects the retail deposits of the bank to grow at a healthy pace.
- **Moderate profitability levels with elevated operating expenses** – DCB remains focussed towards the retail segment which is more operationally intensive. Also, the bank doubled its branch count in the 24 months spanning October 2015 to September 2017. As a result the cost to income ratio of the bank and its operating expenses remain on the higher side. The cost to income ratio and operating expenses as a % of average total assets (ATA) for bank for H1FY2018 was 61% and 3.0% respectively which is higher as compared to the average for private sector banks. The profitability indicator of the bank has thus remained subdued with a return on asset (RoA) and return on equity (RoE) of 0.9% and 10.2% during FY2017. ICRA however expects the operating expenses to moderate as the new branches mature and become more RoE accretive.

Analytical approach:
For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria
ICRA Rating Methodology for Banks
ICRA Rating Methodology for Basel III Compliant Non-Equity Capital Instruments

About the company
Incorporated in 1995, DCB Bank was formed by the merger of Ismailia Co-operative Bank Limited and the Masalawala Co-operative Bank. The Aga Khan Fund for Economic Development (AKFED) and group companies are the largest shareholders in the bank together holding a stake of 15.01%as on September 30, 2017. The bank had a network of 306 branches and 507 ATMs as on September 30, 2017. The bank reported a PAT of Rs 200 crore with a net interest income of Rs. 797 crore in FY2017 compared with a PAT Rs. 195 crore with a net interest income of Rs. 620 crore in FY2016. The bank's total assets stood at Rs. 24,046 crore and its net worth at Rs 1,948 crore as on March 31, 2017.

During H1FY2018, DCB reported a PAT of Rs. 124 crore with a net interest income of Rs. 481 crore vis-a-vis a PAT of Rs. 96 crore with a net interest income of Rs. 367 crore during H1FY2017.

Key Financial Indicators:

	FY2016	FY2017	H1FY2017	H1FY2018
Net Interest Income	620	797	367	481
Profit before tax	261	307	147	195
Profit after tax	195	200	96	124
Net advances	12,921	15,818	14,436	17,395
Total assets	19,119	24,046	21,948	25,908
% CET 1	12.79%	11.87%	10.76%	12.90%
% Tier 1	12.79%	11.87%	10.76%	12.90%
% CRAR	14.11%	13.76%	11.90%	14.65%
% Net Interest Margin / Average total assets	3.94%	4.04%	3.96%	4.22%
% Net Profit / Average total assets	1.14%	0.93%	0.93%	1.00%
% Return on Net Worth	11.59%	10.30%	10.67%	11.28%
% Gross NPAs	1.51%	1.59%	1.75%	1.80%
% Net NPAs	0.75%	0.79%	0.84%	0.90%
% Provision coverage	77.55%	73.80%	75.40%	71.96%
% Net NPA/ Net worth	5.6%	6.4%	6.6%	6.4%

Source: Bank's investor presentation and ICRA research; Amount in Rs. crore
All ratios are as per ICRA calculations

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating history for last three years:
Table:

Sr. No.	Name of Instrument	Current Rating			Chronology of Rating History for the past 3 years					
		Type	Rated amount (Rs. crore)	Nov-17	FY2018	FY2017	FY2016			FY2015
					Nov-17	Nov-16	May-16	Feb-16	Nov-15	Jul-14
1.	Basel III Compliant Tier II Bond Programme	Long Term	550.00	[ICRA] A+ (hyb) (stable)	[ICRA] A+ (hyb) (stable) assigned to Rs. 150 crore bonds programme	[ICRA] A+ (hyb) (stable)	[ICRA] A+ (hyb) (stable) assigned to Rs. 100 crore bonds programme	[ICRA] A+ (hyb) (stable) assigned to Rs. 300 crore bonds programme	-	-
3.	Short Term Fixed Deposits	Short Term	-	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ assigned

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	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Rated Amount (Rs. crore)	Current Rating and Outlook
NA	Basel III Compliant Tier II Bonds Programme	Proposed	-	-	150.00^	[ICRA]A+ (hyb) (stable)
INE503A08010	Basel III Compliant Tier II Bonds Programme	31-Mar-2016	10.25%	30-Apr-2026	86.60	[ICRA]A+ (hyb) (stable)
INE503A08028	Basel III Compliant Tier II Bonds Programme	18-Nov-2016	9.85%	18-Nov-2026	150.00	[ICRA]A+ (hyb) (stable)
NA	Basel III Compliant Tier II Bonds Programme	NA	NA	NA	163.40^	[ICRA]A+ (hyb) (stable)
NA	Short Term Fixed Deposit Programme	NA	NA	NA	NA	[ICRA]A1+

^Yet to be placed
Source: DCB

Contact Details

Analyst Contacts

Karthik Srinivasan
+91 22 61143 444
karthiks@icraindia.com

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

Neha Parikh
+91 22 6114 3426
neha.parikh@icraindia.com

Amaan Elahi
+91 22 6114 3448
amaan.elahi@icraindia.com

Relationship Contact

L. Shivakumar
+91 22 6114 3406
shivakumar@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**

Registered Office
ICRA Limited
1105, Kailash Building, 11th Floor, 26, Kasturba Gandhi Marg, New Delhi 110001
Tel: +91-11-23357940-50, Fax: +91-11-23357014

Corporate Office
Mr. Vivek Mathur
Mobile: +**91 9871221122**
Email: vivek@icraindia.com

Building No. 8, 2nd Floor, Tower A, DLF Cyber City, Phase II, Gurgaon 122002
Ph: +91-124-4545310 (D), 4545300 / 4545800 (B) Fax; +91- 124-4050424

Mumbai **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 3rd Floor, Electric Mansion Appasaheb Marathe Marg, Prabhadevi Mumbai—400025, Board : +91-22-61796300; Fax: +91-22-24331390	**Kolkata** **Mr. Jayanta Roy** Mobile: **+91 9903394664** Email: jayanta@icraindia.com A-10 & 11, 3rd Floor, FMC Fortuna 234/3A, A.J.C. Bose Road Kolkata—700020 Tel +91-33-22876617/8839 22800008/22831411, Fax +91-33-22870728
Chennai **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 5th Floor, Karumuttu Centre 634 Anna Salai, Nandanam Chennai—600035 Tel: +91-44-45964300; Fax: +91-44 24343663	**Bangalore** **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 'The Millenia' Tower B, Unit No. 1004,10th Floor, Level 2 12-14, 1 & 2, Murphy Road, Bangalore 560 008 Tel: +91-80-43326400; Fax: +91-80-43326409
Ahmedabad **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 907 & 908 Sakar -II, Ellisbridge, Ahmedabad- 380006 Tel: +91-79-26585049, 26585494, 26584924; Fax: +91-79-25569231	**Pune** **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 5A, 5th Floor, Symphony, S.No. 210, CTS 3202, Range Hills Road, Shivajinagar,Pune-411 020 Tel: + 91-20- 6606 9999; Fax: +91-20-25561231
Hyderabad **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 4th Floor, Shobhan, 6-3-927/A&B. Somajiguda, Raj Bhavan Road, Hyderabad—500083 Tel:- +91-40-40676500	