Indian Bank

January 12, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Lower Tier-II Bonds	500.00	500.00	[ICRA]AA+(Positive); reaffirmed and outlook revised from Stable
Total	**500.00**	**500.00**	

*Instruments details are provided in Annexure-1

Rating action

ICRA has reaffirmed the [ICRA]AA+ (pronounced ICRA double A plus)[1] rating for the Rs. 500.00 crore[2] Lower Tier-II Bonds of Indian Bank (IB). The outlook on the rating is revised from Stable to Positive.

Rationale

The revision in the outlook factors in a steady reduction in the slippage rate and, improvement in solvency profile, which lends support to its asset quality and capital profile. The fresh slippage rates reduced from 4.6% in FY2016 to 1.7% in H1FY2018 (2.7% in FY2017); ICRA expects the incremental slippage rate to remain moderate as no significant slippages are envisaged from the large account exposures going forward. ICRA however notes that the asset quality indicators are currently subdued with Gross NPAs at 6.7%; it nevertheless compares well vis a vis its peer public sector banks (PSBs). The bank has also improved its provision coverage steady from 38.6% in March 2016 to 50.7% in September 2017 (43.2% in March 2017), which has improved its overall solvency profile and is better placed vis a vis its peers.

The rating continues to factor in the majority Government of India (GoI) ownership (82.1% stake as on September 30, 2017) and the established retail franchise supporting its healthy deposit and liquidity profile. ICRA takes note of the improvement in the profitability indicators over the recent past, supported by the decline in the cost of funds; RoA, although moderate, improved from 0.4% in FY2016 to 0.7% in H1FY2018 (0.7% in FY2017), and its comfortable capitalisation profile (CET-I at 11.3% as on September 30, 2017). Going forward, ability to keep asset quality under control would be crucial from a rating perspective.

Outlook: Positive

The outlook is 'Positive' considering the IB's relatively better position among the public sector banks in terms of asset quality, profitability and capitalisation indicators, which would support in growing its business going forward. The rating would be upgraded if the bank continues to keep asset quality under control and maintain adequate capital and profitability indicators. The outlook would be revised to stable, if the asset quality and earning profile weakens from current levels.

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

[2] *100 lakh = 1 crore = 10 million*

Key rating drivers

Credit strengths

Sovereign ownership – The GoI held 82.1% stake in the bank as on September 30, 2017. While the bank has not received capital from the government in the last two financial years on account of its comfortable capitalisation, ICRA expects the government to support the bank, if required.

Comfortable capitalisation profile - IB's capitalisation profile was comfortable with tier-I and CRAR at 11.7% and 13.2% respectively as on September 30, 2017 as against the minimum tier-I and CRAR requirement of 8.9% and 10.9% respectively by March 31, 2018. As per ICRA's estimates, while the bank does not require any capital during FY2018[3], it would require tier-1 capital (through equity capital or AT-1 bond issuance) at 10-18% of current market capitalization during FY2019. IB's gross advance witnessed good growth of 18.3% (annualised) during H1FY2018 as against modest CAGR of 2.0% during the period FY2015-FY2017. Given the high GoI shareholding and the bank's relatively better profile vis a vis other peer public sector banks, ICRA expects the bank to comfortably meet the capital requirements to support the envisaged credit growth of 15-18%.

Improvement in the solvency profile – The bank has steadily improved its provision cover[4] from 38.6% as on March 31, 2016 (44.5% as on March 31, 2015) to 50.7% as on September 30, 2017 against the PSB average of 45.9% as on September 30, 2017. This has aided the bank in improving its solvency from 40.2% as on March 31, 2016 (25.1% as on March 31, 2015) to 31.1% as on September 30, 2017 against the PSB average of 78.4% as on September 30, 2017.

Established retail franchise with good CASA deposit base - Indian Bank has a long standing presence and established retail franchise in South India with a total branch network of 2,695 as on September 30, 2017. Following the government's demonetisation exercise, the share of CASA deposits in IB's total deposits increased to 37.1% as on March 31, 2017 (36.4% as on September 30, 2017) from 31.3% as on March 31, 2016. The bank also has a good liquidity coverage ratio of 155.7% as on September 30, 2017 as against the regulatory requirement of 90.0% by January 01, 2018.

Credit challenges

Subdued asset quality profile; incremental slippage rates however decline – The bank's gross NPAs increased from 6.7% as on March 31, 2016 (4.4% as on March 31, 2015) to 7.5% as on March 31, 2017 on account of higher slippages and subdued recoveries. During H1FY2018, the asset quality witnessed some improvement with gross NPAs reducing to 6.7% as on September 30, 2017 against the public sector bank (PSB) average of 12.1% as on September 30, 2017 aided by lower incremental slippages. ICRA takes note of the bank's standard restructured advances (excluding state electricity boards and discoms) including SDR, S4A and 5/25 stood at around 2.8% as on September 30, 2017. Going forward, steady improvement in the bank's asset quality indicators would depend on the overall pick up in the business environment and the bank's ability to control incremental slippages and undertake effective recoveries.

Moderate profitability notwithstanding improvement in the recent past – Supported by decline in cost of interest bearing funds, net interest margin improved marginally from 2.3% in FY2016 to 2.5% in FY2017 and further to 2.7% in H1FY2018. With asset quality indicators being largely range-bound, the credit provisions also stood stable at 1.0% during FY2016 and FY2017; however, it has increased to 1.3% during H1FY2018 as the bank strengthened its provision coverage. The treasury income increased from 0.2% in FY2016 to 0.4% in FY2017 and further to 0.5% in H1FY2018 aided by declining bond yield. Thus, the net profitability improved from 0.4% in FY2016 to 0.7% in FY2017 (same for H1FY2018). While the operating profits are expected to remain good for FY2018, the bank would incur higher credit cost during the

[3] Assuming a 2% buffer over regulatory capital levels, 15-18% growth in risk weighted assets and 8-12% internal generation
[4] (Gross NPA – Net NPA) / Gross NPA

year to improve its provision cover. ICRA notes that IB had SRs outstanding at 1.4% of gross advance as on September 30, 2017, on which the bank carries modest provision; this could exert some pressure on the bank' net profitability going forward. Increase in the overall bond yield in the recent past is likely to impact the bank's treasury income in Q3/Q4FY2018. Thus, ICRA expects the bank's profitability indicators are expected to remain largely range-bound, at current levels, for FY2018, however better compared to peer PSBs.

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

About the bank:

Indian Bank is a mid-sized commercial bank, with a majority shareholding by the Government of India (82.1% as on September 30, 2017). The bank had an asset base of about Rs. 2.27 lakh crore (adjusting for the revaluation reserve) and a network of 2,695 branches and 3,202 ATMs as on September 30, 2017. Headquartered in Chennai, IB has a strong presence in South India, which had 62% of its total branches as on September 30, 2017.

Key financial indicators (Audited)

	FY2016	FY2017	H1FY2018
Net Interest Income (Rs. crore)	4,446.2	5,146.1	3,003.1
Profit before Tax (Rs. crore)	955.3	1,758.2	1,167.9
Profit after Tax (Rs. crore)	711.4	1,405.7	823.9
Net advances (Rs. lakh crore)	1.29	1.28	1.39
Total assets (Rs. lakh crore) (adjusted for revaluation reserve)	2.01	2.16	2.27
% CET 1	11.68%	11.82%	11.30%
% Tier 1	12.08%	12.20%	11.66%
% CRAR	13.20%	13.64%	13.16%
% Net interest margin / Average total assets	2.3%	2.5%	2.7%
% Net profit / Average total assets	0.4%	0.7%	0.7%
% Return on net worth	5.3%	9.7%	11.1%
% Gross NPAs	6.7%	7.5%	6.7%
% Net NPAs	4.2%	4.4%	3.4%
% Provision coverage incl technical write-offs	53.4%	58.1%	65.4%
Net NPA / Net worth	40.2%	38.8%	31.0%

Note: Amounts in Rs. crore
Source: Indian Bank, ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

Instrument	Current Rating (FY2018)				Chronology of Rating History for the past 3 years		
	Type	Amount rated (Rs. crore)	Amount Oustanding (Rs. crore)		FY2017	FY2016	FY2015
				Jan-18	Sep-16	Feb-16	Nov-14
Lower Tier II Bonds	Long Term	500.00	500.00	[ICRA]AA+ (positive)	[ICRA]AA+ (stable)	[ICRA]AA+ (stable)	[ICRA]AA+ (positive)

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
INE562A09030	Lower Tier II Bonds	28-Jun-10	8.53%	28-Jun-20	500.00	[ICRA]AA+ (positive)

Source: Indian Bank

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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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