RBL Bank Limited

August 14, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount(Rs. crore)	Current Rated Amount(Rs. crore)	Rating Action
Certificate of Deposit Programme	5,000.00	6,000.00	[ICRA]A1+; Assigned/Outstanding
Basel III Compliant Tier II Bond Programme	800.00	800.00	[ICRA]AA- (hyb) (stable); Outstanding
Medium Term Fixed Deposit Programme	-	-	MAA (stable); Outstanding
Short Term Fixed Deposit Programme	-	-	[ICRA]A1+; Outstanding
Total	**5,800.00**	**6,800.00**	

** Instrument details are provided in Annexure-1*

Rating action

ICRA has assigned the rating of [ICRA]A1+ (pronounced ICRA A one plus) to the Rs. 6,000 crore certificate of deposit programme (enhanced from Rs. 5,000 crore) of RBL Bank Limited (RBL). ICRA has the rating of [ICRA]AA- (hyb) outstanding on the Rs. 800 crore Basel III compliant Tier II bond programme of RBL. ICRA also has the rating of [ICRA]A1+ outstanding on the short-term fixed deposit programme and the rating of MAA outstanding on the medium-term fixed deposit programme of RBL. The outlook on the long-term and medium-term ratings is Stable.

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.

Rationale

The ratings factor in RBL’s steadily improving scale of operations and profitability supported by diversified non-interest income. The ratings are also supported by the comfortable capitalisation levels, the bank’s long track record and its experienced senior management team. The ratings continue to factor in the gradual improvement in the bank’s liability profile supported by the lowering of deposit concentration and improvement in the current and savings account (CASA). Notwithstanding the gradual improvement in its liability profile, the bank’s deposits remained concentrated with a relatively high share of bulk deposits and lower proportion of low-cost deposits in its resource profile. This led to higher cost of funds compared to the average for private banks (PVBs) though the same was comparable to peers. ICRA takes note of the reducing concentration of advances, the bank’s top-20 group exposures stood at 21% of the total exposures and 217% of Tier I capital as on March 31, 2018 compared to 25% and 314% respectively as on March 31, 2016. ICRA also notes that the top-20 group exposures were towards corporates with good credit quality. Given the robust growth in the last four years, the bank’s loan book is relatively unseasoned with a high share of unsecured portfolio (~33% of advances & 37% of exposures as on June 30, 2018); 9% of the unsecured book is in the form of microfinance loans where the borrower profile is vulnerable to economic shocks.

Outlook: Stable

The Stable outlook factors in ICRA’s expectations that the bank will continue maintaining strong asset quality while improving the diversity in the asset and liability profile. Further, supported by the steady growth in core earnings, ICRA expects continued improvement in the profitability levels. Though the bank will require to raise capital during the next

18-24 months to support growth, it is well-placed in terms of its ability to raise capital. The ability to diversify the mix of assets and liabilities, while it maintains a comfortable asset quality and capitalisation will remain a key rating positive. Conversely, a sharp deterioration in the asset quality as the loan book seasons leading to a decline in profitability or an increase in the concentration of exposures or liabilities will be rating negatives.

Key rating drivers

Credit strengths

Steadily improving scale of operations - The bank's loan book grew by 37% YoY to Rs. 40,268 crore as on March 31, 2018 and further by 36% YoY to Rs. 42,198 crore as on June 30, 2018. This is in line with the bank's medium-term plans of growing the loan book at a CAGR of 30-35% till FY2020. Within the loan book, the share of non-wholesale advances stood at 41% as on June 30, 2018 (39% as on March 31, 2017). Growth in non-wholesale advances was supported by retail assets (YoY growth of 45%) across segments and micro banking (up 66% YoY), which was driven by the business correspondent (BC) branch expansion. Within the wholesale segment, the bank largely caters to the short-term working capital requirements of corporate customers. Of the total loan book, 71% of the advances were of less than 1-year tenure while 87% was in the less than 3-year tenure bracket as on June 30, 2018. Of the total portfolio, 67% of the portfolio was secured as on June 30, 2018 (68% as on March 31, 2017). The unsecured portfolio includes loans to micro-loan borrowers, business loans, credit card as well as bank lines for certain highly rated large corporate borrowers.

Capitalisation profile remains comfortable – The bank reported comfortable capitalisation with Tier I and CRAR as a percentage of risk weighted assets (RWA) of 13.1% and 14.6% respectively as on June 30, 2018 (11.4% and 13.7% respectively as on March 31, 2017). The bank last raised capital through a preferential issue of Rs. 1,680 crore in August 2017 which helped in boosting the capitalisation. The solvency remained strong with net NPAs/net worth of 4.6% as on June 30, 2018 (4.4% as on March 31, 2017) and was better than the industry average. With quarterly capital consumption of ~40-45 bps of Tier I, the bank would require to raise capital in the medium term (before March 2020 as per ICRA's assessment). In ICRA's view, the bank is well-placed in terms of its ability to raise capital.

Steady improvement in profitability driven by lower cost of funds - The yield on advances declined to 9.8% during FY2018 (10.4% in FY2017). However, with a higher decline in the cost of interest bearing funds to 5.7% during FY2018 (6.4% in FY2017), the bank's net interest margins[1] (NIMs) improved to 3.2% during FY2018 (2.8% in FY2017). ICRA notes that the surplus liquidity conditions during a large part of FY2018 and the higher share of bulk deposits have contributed to the higher decline in the bank's cost of funds compared to PVB averages. With the improvement in NIMs and the significant growth in advances, the bank's net interest income (NII) registered a YoY growth of 45% during FY2018 (49% in FY2017). Strong NII growth and increasing non-interest income of 1.6% of ATA during FY2018 (1.4% in FY2017) translated into improving operating profitability of 2.1% of ATA during FY2018 (1.8% during FY2017). This was partially offset by higher credit provisions on micro-finance and agriculture segments of 0.7% of ATA during FY2018 (0.5% during FY2017) resulting in a limited improvement in profit after tax (PAT) / ATA to 1.1% in FY2018 compared to 1.0% in FY2017. During Q1FY2019, PAT/ATA improved further to 1.2% supported by higher NIMs (yields increased with the increase in the MCLR and the change in the portfolio mix towards higher-yielding non-wholesale advances) and lower operating expenses.

Comfortable asset quality - With slippages in the micro-finance loans (part of the Development Banking and Financial Inclusion (DB&FI) segment) post demonetisation and higher slippages in the agri portfolio, the bank's asset quality weakened with gross NPAs (GNPAs) increasing to 1.40% as on March 31, 2018 (1.20% as on March 31, 2017). The asset quality has stabilised with GNPAs of 1.40% as on June 30, 2018, as incremental movement to higher overdue buckets in

[1] as a percentage of average total assets (ATA)

micro loans has reduced and overdues have stabilised. With a provision cover ratio (PCR) of 47%, the net NPAs stood at 0.75% as on June 30, 2018 (PCR of 47% and net NPA of 0.64% as on March 31, 2017). The bank's standard restructured assets stood limited at 0.10% of the total advances as on June 30, 2018 (0.25% as on March 31, 2017). RBL's security receipts were also limited at 0.06% of the total advances as on June 30, 2018. Moreover, the bank does not have any exposure to the accounts identified by the Reserve Bank of India for insolvency proceedings.

Comfortable Liquidity - The bank's liquidity remains comfortable with 1 year negative structural liquidity gaps of 0.32% of outflows as on June 30, 2018. The bank's comfortable liquidity coverage ratio (100.75% as on June 30, 2018 against the regulatory requirement of 90% as on January 01, 2018 and 100% as on January 1, 2019) provides further comfort.

Credit challenges

Albeit an improvement, resource profile remains concentrated – Notwithstanding the gradual improvement, the bank's deposit profile is concentrated as reflected in the 70% share of bulk deposits (deposits over Rs. 1 crore) as on March 31, 2018 (as compared to 72% as on March 31, 2016). The top-20 depositors also remained concentrated at 19.27% of total deposits as on March 31, 2018 as compared to 21.41% as on March 31, 2017. Even though the bank's Current Account and Saving Account (CASA) ratio improved to 24.4% as on June 30, 2018 from 18.6% as on March 31, 2016, the ratio remains lower than that of many other PVBs and the banking sector average. The increase in RBL's savings deposits was because of the higher rates offered on the same, improved visibility on the bank through an increasing branch presence and branding efforts, and partly because of demonetisation. While the buildup in savings accounts has been slower for the bank in the last two quarters, this has largely been because of management's focus on building the lower ticket savings accounts. With a high share of bulk deposits and surplus liquidity conditions the cost of interest bearing funds declined to 5.7% during FY2018 from 6.4% during FY2017, though it remained above the PVB average of 5.3% and 5.8% respectively. Ability to further granulise the liability profile, and maintain competitive cost of funds in tighter liquidity situations will be important drivers for sustained profitability.

Concentration of advances, albeit gradually reducing - RBL's top 20-group exposures accounted for 23% of the total exposures and 216% of Tier I capital as on March 31, 2018 compared to 25% and 314% respectively as on March 31, 2016. The top 20-single borrower exposure accounted for 11.7% of the total exposure as on March 31, 2018 compared to 13.42% as on March 31, 2016. The concentration is gradually reducing and the top borrower groups are higher rated corporates groups which provides some comfort. The bank's operations were initially concentrated in the Maharashtra and North Karnataka regions. In the past six years, it has opened branches in commercial zones like Delhi, Chennai and other metros. Exposures in these branches have started increasing, resulting in lower geographic concentration. As on March 31, 2018, the western region accounted for 42% of net advances (38% in March 31, 2017) followed by 22% in the North (25%), 19% in South (21%) and 17% in East (16%).

Higher credit risk on unsecured and agri portfolio - Following demonetisation, the bank's asset quality of micro-loans in the DB&FI segment suffered the most given the unsecured nature of lending and the marginal profile of the borrowers. The high delinquencies led to high credit provisioning for the bank during FY2018. The bank has provided for two third of the stressed portfolio till June 2018 and the balance is to be provided in FY2019. Since RBL's direct microfinance lending is sourced through business correspondents (BCs), it has first loss default guarantees (FLDG) of 3-5% on its microfinance book furnished by the BCs which partly mitigates the loss. Further, the bank's agri portfolio (~4% of total advances) was impacted by farm loan waivers. With the high share of the unsecured portfolio (33% as on June 30, 2018), the portfolio is exposed to credit risk. The credit provisions stood at 0.7% of ATA during FY2018 (0.5% during FY2017) but is expected to decline during FY2019 as the incremental slippage ratio is expected to be lower than the FY2018 level.

Operating expenses remain high – Despite the strong growth in NII, improvement in NIMs and the increasing share of non-interest income, the bank's operating cost-to-income ratio[2] was high at 56.7% in FY2018 (57.3% in FY2017), surpassing the private sector banks' average of 46.1% in FY2018. The bank's operating expenses are expected to remain high with significant investments being made in infrastructure, branches and technology in line with the scaling up of operations. Because of the high cost-income ratio, the bank's operating profitability remains below PVB averages. However, supported by the comfortable asset quality and controlled credit costs, the net profitability (PAT/ATA) stands comparable to PVB averages.

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 company:

RBL Bank Limited is a Kolhapur, Maharashtra based private sector bank established in 1943. Following a management change in 2010, the bank's corporate office shifted to Mumbai. Since FY2011, it is one of the fastest growing scheduled commercial banks with a presence across 16 Indian states and union territories. As on June 30, 2018, RBL operated through 266 branches, 199 banking outlets, 847 business correspondent branches (including banking outlets) and 369 ATMs.

Key financial indicators (Audited)

	FY2017	FY2018	Q1FY2018	Q1FY2019
Net interest income	1,221	1,766	378	553
Profit before tax	681	967	217	292
Profit after tax	446	635	141	190
Net advances	29,449	40,268	31,108	42,198
Total assets	48,675	61,851	48,855	62,563
% CET 1	11.40%	13.61%	11.10%	13.10%
% Tier 1	11.40%	13.61%	11.10%	13.10%
% CRAR	13.72%	15.33%	13.40%	14.60%
% Net interest margin / Average total assets	2.78%	3.20%	3.10%	3.55%
% Net profit / Average total assets	1.02%	1.15%	1.16%	1.22%
% Return on net worth	13.46%	11.53%	12.92%	11.20%
% Gross NPAs	1.20%	1.40%	1.46%	1.40%
% Net NPAs	0.64%	0.78%	0.80%	0.75%
% Provision coverage excl. technical write offs	46.77%	57.57%	57.99%	60.41%
% Net NPA/ Net worth	4.38%	4.68%	5.69%	4.58%

Amount is Rs. crore; All ratios are as per ICRA calculations
Source: RBL; ICRA Research

[2] *Trading income is excluded from operating income, for computing the operating cost to income ratio*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2019)				Chronology of Rating History for the past 3 years						
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)		FY2018		FY2017			FY2016	
					Aug-18	Jan-18	Oct-17	Mar-17	Dec-16	July-16	Feb-16	Jul-15
1	Certificate of Deposits	Short Term	6,000.00	NA	[ICRA] A1+ assigned	[ICRA] A1+	[ICRA] A1+	[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); upgrade from [ICRA]A+ (hyb) (positive)	[ICRA]A+ (hyb) (positive); outlook revised to positive	[ICRA] A+ (hyb) (stable)	[ICRA]A+ (hyb) (stable)	[ICRA]A+ (hyb) (stable); Assigned	NA
4	Medium Term Fixed Deposits	Medium Term	-	-	MAA (stable)	MAA (stable)	MAA (stable); upgraded from MAA- (positive)	MAA- (positive); outlook revised to positive	MAA- (stable)	MAA- (stable)	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 No	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	Certificate of Deposits	-	-	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.

For more information, visit www.icra.in

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