

October 28, 2022

## Bandhan Bank Limited: Ratings reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
NCD programme	110.00	110.00	[ICRA]AA (Negative); reaffirmed
	86.40	-	[ICRA]AA (Negative); reaffirmed and withdrawn
Term loans	80.00	80.00	[ICRA]AA (Negative); reaffirmed
Certificates of deposit	3,000.00	3,000.00	[ICRA]A1+; reaffirmed
<b>Total</b>	<b>3,276.40</b>	<b>3,190.00</b>	

\*Instrument details are provided in Annexure I

### Rationale

The ratings reaffirmation continues to factor in Bandhan Bank Limited's (Bandhan) comfortable capitalisation levels with a Tier I capital ratio of 18.30% as on June 30, 2022, though the same declined from the higher levels in the past because of the growth amidst weaker internal accruals. Besides this, Bandhan benefits from its strong liquidity profile, supported by its steadily increasing and granular deposit base, with a high share of retail depositors.

While the emerging entrepreneur business (EEB) portfolio has supported the high profitability levels, post the Covid-19 pandemic, the gross stressed pool in the EEB segment (gross non-performing advances (GNPAs) + gross restructured + SMA<sup>1</sup> 1 + SMA 2) remained elevated at Rs. 12,120 crore or 20.9% of the EEB portfolio as on June 30, 2022. However, the same has moderated from the peak of Rs. 19,457 crore or 36.0% of the EEB portfolio as on September 30, 2021, as a significant part of this stressed book slipped, resulting in elevated credit costs. Including the non-EEB portfolio, the gross stressed book stood at Rs. 14,929 crore or 15.5% of gross advances as on June 30, 2022. The bank has steadily increased the provision on its stressed book and, net of provisions, the stressed book stood at Rs. 6,029 crore or 6.6% of net advances as on June 30, 2022. Despite the reduction, the net stressed book remains elevated, thereby driving the Negative outlook on the rating. ICRA expects that the net stressed pool of assets shall gradually reduce in the near term. However, the bank's ability to reduce this through collections/recoveries remains to be seen as it will be a critical driver of its profitability and capital cushions.

ICRA has withdrawn the rating on Bandhan's Rs. 86.40-crore non-convertible debenture (NCD) programme as the same has been fully redeemed with no amount outstanding against the rated instrument. The rating has been withdrawn as per ICRA's policy on the withdrawal and suspension of credit ratings ([click here for the policy](#)).

### Key rating drivers and their description

#### Credit strengths

**Higher share of unsecured/microfinance loans leads to strong operating profits** – The bank has a long track record in the microfinance industry and has operational experience of more than two decades. Consequently, it has high customer vintage, loyalty and a strong connect with its microloan customers. It has demonstrated resilient asset quality during events such as demonetisation and the Assam agitation, which disrupted the microfinance industry. However, the pandemic has severely impacted the debt-servicing ability of borrowers and, hence, the asset quality of the bank. While Bandhan has diversified into

<sup>1</sup> Special mention accounts (SMA) are overdue loans with SMA 0 reflecting an overdue status of up to 30 days, SMA 1 reflecting an overdue status of 31-60 days and SMA-2 reflecting an overdue status of 61-90 days

secured lending through its merger with GRUH Finance Limited in FY2020, microloans (or EEB segment) continued to account for 60% of its loan portfolio as on June 30, 2022.

Furthermore, the higher level of non-interest income (NOI), driven by income from the sale of priority sector lending certificates (PSLCs), has historically supported the operating profitability. However, following directives from the Reserve Bank of India (RBI) regarding the reclassification of eligible loans, the NOI from the sale of PSLCs will decline. ICRA has highlighted this vulnerability in its previous rationales. Despite the anticipated reduction in the NOI, Bandhan's profitability metrics are expected to remain strong. Nevertheless, its presence in the microloan segment with a marginal borrower profile, which makes the portfolio vulnerable to episodic events, may translate into higher credit costs.

**Comfortable capital position; ability to meet targeted recovery from stressed pool and various government schemes available on stressed pool remains monitorable** – The bank reported a Tier I ratio of 18.30% as on June 30, 2022, which declined from 23.85% as on June 30, 2021 because of the increasing loan book, while capital accretion remained muted on account of elevated credit costs. Bandhan last raised equity capital of Rs. 3,662 crore in FY2018 and since then, its capital position has largely been supported by internal accruals.

Given its growth plans, Bandhan's ability to maintain and improve its capitalisation profile would remain contingent upon the restoration of its profitability, which will remain a function of lower credit costs. The bank expects credit provisions to remain at 2.5% or Rs. 2,500-3,000 crore of advances in FY2023, which is lower than Rs. 11,791 crore (17.7% of advances as on March 31, 2020) incurred during FY2021-FY2022. This will be driven by the reduction in the net stressed book and improved collections, apart from recoveries under various government schemes.

**Healthy growth in deposits with higher share of retail deposits** – The overall deposit base expanded by 20.3% year-on-year (YoY) to Rs. 93,057 crore as on June 30, 2022. Furthermore, the growth in the deposit franchise in recent years was driven by retail deposits, with retail current account savings account (CASA) + retail term deposits growing by 11.5% YoY as on June 30, 2022 and accounting for 84.4% of the total deposits as on June 30, 2022 (growth of 21.2% in FY2022 and accounting for 77.3% as on March 31, 2022). Moreover, the bank's overall CASA level remained in line with the private sector average, which stood at 45.6% as on June 30, 2022. Supported by the surplus liquidity environment during the last two years, the gap between the cost of interest-bearing funds for Bandhan and the private sector average has narrowed. However, the ability to maintain this in a tighter liquidity environment may be a challenge for the bank.

## Credit challenges

**Net stressed portfolio remains high despite moderation from peak level; asset quality remains a monitorable, given the presence in marginal borrower profile segment** – With a significant presence in the unsecured micro-banking segment and the impact of the pandemic, the fresh NPA generation rate remaining elevated for the bank at more than 10% during FY2021-FY2022. The GNPA's and net NPAs (NNPAs) rose to a lifetime high of 10.82% and 3.04%, respectively, as on September 30, 2021. In response, Bandhan undertook accelerated provisions and write-offs, which supported the headline asset quality numbers. In Q1 FY2023, floods in Assam (accounting for ~9% of EEB book) and the weak performance of the restructured book exiting the moratorium led to a sequential weakening in the asset quality metrics with the GNPA% and NNPA% at 7.25% and 1.92%, respectively, as on June 30, 2022 compared with 6.46% and 1.66%, respectively, as on March 31, 2022.

Overall, the stressed pool in the EEB segment (GNPA + gross restructured + SMA 1 + SMA 2) was high at Rs. 12,120 crore or 20.9% of the EEB portfolio as on June 30, 2022, while the gross stressed pool, inclusive of the non-EEB book, stood at Rs. 14,929 crore or 15.5% of gross advances as on June 30, 2022. Net of the provisions, the stressed book at the bank level stood at Rs. 6,029 crore or 6.7% of standard advances or 33.4% of the Tier I capital as on June 30, 2022 (16.6% of standard advances and 84.2% of Tier I capital as on September 30, 2021). While there has been a relative moderation in the stress position, it remains meaningfully high.

**High geographical concentration of loan portfolio** – While Bandhan has increased its pan-India presence across 34 states and Union Territories (UTs), 57% of the banking outlets were in the eastern and north-eastern regions as on June 30, 2022. Its advances and deposits have high geographical concentration in the eastern and north-eastern regions of India, specifically West Bengal and Assam, owing to the concentration of the branch network. This exposes the bank to event risks and economic

conditions, especially in these geographies. Recently, floods in Assam also led to a lower collection efficiency and higher slippages/overdues book, given the meaningful share of the state in overall advances. Following the merger with GRUH, the bank's geographical presence has seen some diversification, given its presence in 11 states and one UT through 195 GRUH centres, most of which are in the western part of India. However, ICRA expects the portfolio concentration to continue in these regions in the medium term, given the size of the existing portfolio and the branch network.

## Environmental and social risks

**Environmental considerations** – Given the service-oriented business of Bandhan, its direct exposure to environmental risks as well as those emanating from regulations or policy changes is not material. While the bank does not face material physical climate risks, it is exposed to environmental risks indirectly through its portfolio of assets. For instance, the bank has ~12% exposure towards the agriculture segment, which remains vulnerable to climate-related adversities. However, such risk is unlikely to be material because the bank benefits from portfolio diversification. Further, the lending is usually short-to-medium term, which allows the bank to adapt while taking incremental exposures on less environmentally vulnerable businesses.

**Social considerations** – Data security and customer privacy are among the key sources of vulnerability for Bandhan as any material lapse could be detrimental to its reputation and could invite regulatory censure. Customer preference is increasingly shifting towards digital banking, which provides an opportunity to reduce the operating costs. However, the possibility of sub-par execution of the information technology strategy, and thus the inability to adequately meet the customers' needs, could result in more costs than benefits.

On the positive side, Bandhan contributes towards enhancing financial inclusion by providing several products and services that are specifically targeted towards the marginalised sections of society and attempts to address and cater to social concerns. Prudent lending to such under-served segments could create growth opportunities. However, such growth opportunities must be seen in conjuncture with asset quality risks that could impact the bank's credit quality.

## Liquidity position: Strong

The bank reported a positive cumulative gap across all maturity buckets as per the structural liquidity statement as on June 30, 2022. Bandhan's largely stable deposit profile, coupled with the short tenure of microloans (12-24 months), largely supported its strong liquidity profile. The daily average liquidity coverage ratio (LCR) remained strong at 134.6% for Q1 FY2023, while the net stable funding ratio (NSFR) stood at 124.6%, with both remaining above the regulatory level of 100%. Bandhan is estimated to have excess statutory liquidity ratio (SLR) securities of ~Rs. 14,000 crore (15.0% of deposits), as on June 30, 2022, which can be sold to meet its liquidity requirements. Additionally, it reported a sizeable cash and bank balance of Rs. 8,992 crore or 6.4% of the total assets as on June 30, 2022. Moreover, Bandhan's ability to avail refinance and undertake inter-bank participation certificate (IBPC) transactions, given that a significant share of its portfolio qualifies for PSL, enhances its liquidity.

## Rating sensitivities

**Positive factors** – ICRA could revise the outlook to Stable if the bank is able to reduce its net stressed assets portfolio (NPA + restructured + SMA1 + SMA2) to less than 3% of advances, improve its profitability with a return on assets (RoA) of >3% and maintain the Tier I capital position above 20%.

**Negative factors** – ICRA could downgrade the ratings if the net stressed book (NPA + restructured + SMA1 + SMA2) remains elevated at >5%, leading to continued uncertainty on the asset quality, capital and profitability. A decline in the Tier I ratio below 15% will also be a negative rating trigger.

## Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	<a href="#">ICRA Rating Methodology for Banks</a> <a href="#">Policy on Withdrawal of Credit Ratings</a>
Parent/Group support	Not Applicable
Consolidation/Standalone	The ratings are based on the standalone financials of Bandhan

## About the company

Erstwhile Bandhan Financial Services Private Limited (BFSL) was the largest non-banking financial company-microfinance institution (NBFC-MFI) in India and the first entity to receive an in-principle universal banking licence from the RBI. Following the transfer of BFSL's business to the bank, Bandhan Bank Limited (Bandhan) commenced operations in August 2015.

Bandhan was incorporated in December 2014 as a wholly-owned subsidiary of Bandhan Financial Holdings Limited (BFHL). On August 3, 2020, BFHL diluted its shareholding in Bandhan to 40% to comply with the regulatory requirement on promoter holding in the bank. BFHL's stake was diluted to 82.28% upon the initial public offer by Bandhan in March 2018 and later to 60.96% upon the amalgamation with GRUH in October 2019. BFHL is now required to further reduce its shareholding in the bank to 15% by August 2027.

BFSL holds 100% equity in BFHL. BFSL's shareholders are Financial Inclusion Trust (FIT; 32.91%), Caladium Investment Pte Ltd (16.7%), International Finance Corporation (13.59%), IFC FIG Investment Company (2.85%), Bandhan Employee Welfare Trust (14.61%), Small Industries Development Bank of India (SIDBI; 8.13%), North East Financial Inclusion Trust (NEFIT; 7.82%), and individuals (3.4%). FIT and NEFIT are trusts formed in FY2009 with corpus donations from Bandhan Konnagar, the non-governmental organisation (NGO) from which the microfinance portfolio was transferred to BFSL. The beneficiaries of these trusts are the public while the trustees are industry professionals.

Bandhan has its headquarters in Kolkata and follows the group-based individual lending model for the microfinance business. The amalgamation of GRUH (housing finance company) with Bandhan was completed in 2019. GRUH had a presence in 11 states and one UT through 195 GRUH centres, most of which are in the western part of India. As on June 30, 2022, Bandhan had a network of 5,639 branches, banking units or doorstep service centres (DSCs) and GRUH centres, spread across 34 states and UTs.

## Key financial indicators (audited)

Bandhan Bank	FY2021	FY2022	Q1 FY2022	Q1 FY2023
Net interest income	7,563	8,714	2,114	2,514
Profit before tax	2,949	129	496	1,178
Profit after tax	2,205	126	373	887
Net advances	81,613	93,975	74,766	90,883
Total assets	1,14,987	1,38,867	1,10,399	1,41,235
CET I/Tier I	22.48%	18.90%	23.85%	18.30%
CRAR	23.47%	20.10%	24.81%	19.40%
Net interest margin	7.32%	6.87%	7.50%	7.18%
PAT/ATA	2.13%	0.10%	1.32%	2.53%
Return on net worth	12.67%	0.72%	8.48%	19.89%
Gross NPAs	6.81%	6.46%	8.18%	7.25%
Net NPAs	3.51%	1.66%	3.29%	1.92%
Provision coverage excl. technical write-offs	50.31%	75.48%	61.84%	74.90%
Net NPA/Core equity capital	16.95%	9.13%	14.75%	13.28%

Note: Amount in Rs. crore; All calculations are as per ICRA Research  
Total assets and net worth exclude revaluation reserves  
Quarterly results are unaudited; annual results are audited  
Source: Bandhan Bank, ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

### Rating history for past three years

	Instrument	Current Rating (FY2023)			Date & Rating in FY2023	Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Oct 28, 2022 (Rs. crore)		Date & Rating in FY2022	Date & Rating in FY2021		Date & Rating in FY2020
							Feb 24, 2021	Aug 10, 2020	
1	Term loans*	Long term	80.00	Nil	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
2	Certificates of deposit	Short term	3,000.00	1,400.00^	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
3	Non-convertible debenture programme	Long term	110.00	110.00	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable); Assigned
4	Non-convertible debenture programme	Long term	86.40	-	[ICRA]AA (Negative); reaffirmed and withdrawn	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable); Assigned
5	Non-convertible debenture programme	Long term	-	-	-	-	[ICRA]AA (Stable); reaffirmed and withdrawn	[ICRA]AA (Stable)	[ICRA]AA (Stable); Assigned
6	Subordinated Tier II NCD	Long term	-	-	-	[ICRA]AA (Negative); reaffirmed and withdrawn	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)

\*The amount is yet to be allocated

<sup>^</sup> Data as on October 19, 2022

### Complexity level of the rated instruments

Instrument	Complexity Indicator
NCD programme	Very Simple
Term loans	Simple
Certificates of deposit	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: [www.icra.in](http://www.icra.in)

## Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term loans*	NA	NA	NA	80.0	[ICRA]AA (Negative)
INE580B07455	Non-convertible debentures^	Oct-30-2018	9.50%	Oct-30-2028	75.0	[ICRA]AA (Negative)
INE580B07489	Non-convertible debentures^	Dec-06-2018	9.35%	Oct-31-2023	35.0	[ICRA]AA (Negative)
INE545U16426	Certificates of deposit	Sep-29-2022	7.60%	Sep-29-2023	200.00	[ICRA]A1+
INE545U16426	Certificates of deposit	Sep-29-2022	7.60%	Sep-29-2023	50.00	[ICRA]A1+
INE545U16418	Certificates of deposit	Sep-12-2022	7.10%	Sep-12-2023	25.00	[ICRA]A1+
INE545U16418	Certificates of deposit	Sep-12-2022	7.10%	Sep-12-2023	100.00	[ICRA]A1+
INE545U16418	Certificates of deposit	Sep-12-2022	7.10%	Sep-12-2023	200.00	[ICRA]A1+
INE545U16384	Certificates of deposit	Mar-31-2022	5.80%	Mar-15-2023	200.00	[ICRA]A1+
INE545U16384	Certificates of deposit	Mar-30-2022	5.80%	Mar-15-2023	100.00	[ICRA]A1+
INE545U16384	Certificates of deposit	Mar-17-2022	5.80%	Mar-15-2023	100.00	[ICRA]A1+
INE545U16384	Certificates of deposit	Mar-15-2022	5.80%	Mar-15-2023	50.00	[ICRA]A1+
INE545U16384	Certificates of deposit	Mar-15-2022	5.80%	Mar-15-2023	300.00	[ICRA]A1+
INE545U16384	Certificates of deposit	Mar-15-2022	5.80%	Mar-15-2023	75.00	[ICRA]A1+
NA	Certificates of deposit	NA	NA	7-365 days	1,600.0	[ICRA]A1+
INE580B07497	Non-convertible debentures^	Nov-28-2018	9.18%	Mar-29-2022	86.4	[ICRA]AA (Negative); reaffirmed and withdrawn

\*The amount is yet to be allocated; ^ These NCDs were transferred to Bandhan from erstwhile GRUH Finance Limited as a part of the amalgamation

Source: Bandhan Bank, ICRA Research

## Annexure II: List of entities considered for consolidated analysis – Not applicable

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