August 11, 2023

Small Industries Development Bank of India: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term bonds programme	38,015	38,015	[ICRA]AAA (Stable); reaffirmed
Long-term bonds programme	620	-	[ICRA]AAA (Stable); reaffirmed & withdrawn
Total	**38,635**	**38,015**	

**Instrument details are provided in Annexure I*

Rationale

The rating for Small Industries Development Bank of India (SIDBI) factors in its position as an apex financial institution (FI) for the promotion and development of the micro, small and medium enterprise (MSME) sector in India. SIDBI was established under an Act of Parliament in 1990 and is jointly owned by the Government of India (GoI; 20.85%), public sector banks (PSBs), insurance companies and other FIs as on March 31, 2023.

To enhance SIDBI's competitive funding position, the GoI facilitates access to low-cost micro and small enterprise (MSE) funds[1] for onward refinancing to eligible lending institutions at competitive rates. The allocation for FY2024 stood at Rs. 75,000 crore (over and above deposits of Rs. 9,000 crore, which were not received in FY2023), which is higher than the allocation for previous years, and is available at a concessional interest rate. These MSE funds accounted for 43% of SIDBI's total borrowings as on March 31, 2023 and supported the competitive cost of funds for the bank.

As a part of its lending operations and refinancing activities, SIDBI takes exposure to scheduled commercial banks (SCBs), private entities other than banks, and non-banking financial companies (NBFCs). Some of the counterparties, especially in the direct lending segment, could be weak while a few lumpy NBFC exposures have slipped in recent years, resulting in a relative increase in the overall slippages during these years. However, SIDBI has largely provided for these exposures and the headline asset quality metrics remain strong with the net non-performing advances (NPAs) at 0.01% as on June 30, 2023 (0.00% as on March 31, 2023 and 0.07% as on March 31, 2022).

Given the sharp growth, partly driven by higher refinancing requirements due to tightening liquidity conditions, SIDBI's leverage[2] rose to 14.36 times as on March 31, 2023 (9.22 times as on March 31, 2022) but remained within the regulatory permissible level. Going forward, its borrowings are likely to increase, and the leverage is expected to rise, although it is likely to remain within the allowed limit of 18 times till March 31, 2024. SIDBI's capitalisation level remains comfortable with a capital-to-risk weighted assets ratio (CRAR) of 15.63%[3] as on June 30, 2023 (19.29% as on March 31, 2023 and 24.28% as on March 31, 2022), which is supported by the lower risk weights for the refinance book. SIDBI has a superior liquidity profile with positive asset-liability gaps in the short as well as long term, which are supported by the matching tenure of the assets (refinancing loan book) and the liabilities (MSE funds). The liquidity profile is further supported by standby lines from banks, including the pending drawdown against the allocated MSE fund.

[1] MSE fund is created out of deposits from SCBs against their shortfall in priority sector lending (PSL) targets
[2] Leverage = Total debt/Net owned funds; As per Reserve Bank of India (RBI) regulations, All India Financial Institutions (AIFIs) have to maintain a leverage of 10 times, though SIDBI has received approval for a higher leverage of 18 times till March 31, 2024
[3] CRAR as on June 30, 2023 does not include profits for the first quarter, if included, CRAR stands at 18.5%

ICRA expects that SIDBI will continue to benefit from its role of an apex FI for the development of the MSME sector and its strategic importance to the GoI, driving the Stable outlook on the rating. Given the cap on the lending margins, the earnings profile in terms of return on assets/equity (RoA/RoE) is likely to remain modest, though the profitability is expected to be sufficient for achieving the targeted growth without fresh equity capital requirements in the near to medium term.

ICRA has withdrawn the rating assigned to the Rs. 620.00-crore long-term bonds as they have matured. The rating was withdrawn in accordance with ICRA's policy on withdrawal of credit ratings (ICRA's Policy on Withdrawal).

Key rating drivers and their description

Credit strengths

Strategic importance to GoI for development of MSME sector – SIDBI is an FI established in 1990 under an Act of Parliament (SIDBI Act, 1989). Under the Act, SIDBI has been described as a development bank established as 'the principal financial institution for the promotion, financing and development of industry in the small-scale sector and to coordinate the functions of the institutions engaged in the promotion, financing or developing of industry in the small-scale sector and for matters connected therewith or incidental thereto'.

Tier I capital bonds amounting to Rs. 1,423 crore were converted into equity share capital in FY2022, resulting in an increase in the GoI's share to 20.85% as on March 31, 2022 from 15.40%. Besides this, State Bank of India {SBI; [ICRA]AAA (Stable)}, which has the second highest shareholding in SIDBI, had a stake of 15.65% while the share of Life Insurance Corporation of India (LIC) stood at 13.33% as on March 31, 2023. The rest is held by other PSBs and institutions.

Despite the relative increase in the GoI's stake, ICRA notes that the overall shareholding remains fragmented. Hence, in the absence of a single dominant shareholder or promoter, future capital raising, if any, will remain dependent on the ability and willingness of all the shareholders to contribute capital in a timely manner. Nevertheless, given the regulatory dispensation on the leverage and the expected internal capital generation in FY2024, the requirement for capital support remains limited in the near to medium term.

Strong asset quality indicators – SIDBI's refinance portfolio accounted for 83.65% of the total net advances as on March 31, 2023 (82.48% as on March 31, 2022). Slippages have remained low, given the significant share of the refinance segment, which consists of banks and high rated NBFCs. However, SIDBI has witnessed slippages from its NBFC exposures in the past. As a result, the fresh NPA generation rate stood at 0.05% in FY2023, which was lower than 0.66% in FY2022. The gross NPA (GNPA) and NNPA ratios also remained strong at 0.01% and 0.00%, respectively, as on March 31, 2023 (0.11% and 0.07%, respectively, as on March 31, 2022 and 0.18% and 0.12%, respectively, as on March 31, 2021).

The asset quality indicators in the direct lending book had been comparatively weaker than the refinance book in the past, although the impact on the overall asset quality metrics has been limited as the total share in advances was low at 0.01% as on June 30, 2023 (0.00% as on March 31, 2023).

Funding profile remains strong with MSE fund allocations – SIDBI's funding profile remains dominated by low-cost MSE Refinance fund allocations. It has access to these low-cost funds, which are made available by banks against their shortfalls in meeting their priority sector lending (PSL) targets. The total borrowings under the MSE fund programme remained at Rs. 1.57 lakh crore and comprised 46% of the overall borrowings as on March 31, 2023. Given its quasi-sovereign status, SIDBI mobilises funds at competitive rates from the capital markets in the form of bonds, commercial papers and certificates of deposit.

Given the expected growth in advances, the MSE Refinance allocation for FY2024 was higher at Rs. 84,000 crore (including Rs. 9,000 crore of previous allocations) compared to Rs. 65,000 crore in FY2023 and Rs. 55,000 crore in FY2022. In addition to this, SIDBI had an undrawn allocation of Rs. 3,900 crore in FY2023 under the Cluster Development Fund. Continued allocations under MSE funds will remain important for SIDBI for maintaining a competitive cost of funds as well as the scale of its refinancing business and hence its profitability. Given the growth targets for FY2024, the RIDF allocations are expected to remain the dominant source of funding for SIDBI.

Capitalisation metrics comfortable, although leverage relatively elevated – As liquidity conditions tightened in FY2023, refinancing requirements/demand rose, which supported SIDBI's strong book growth in FY2023. As a result, the overall leverage increased to 14.36 times as on March 31, 2023 from 9.22 times as on March 31, 2022 and 7.91 times as on March 31, 2021. Given the plans to grow its total assets by ~25% in FY2024 and the permissible leverage of 10 times for FIs, SIDBI has received the Reserve Bank of India's (RBI) approval to borrow up to 18 times of its net owned fund (NOF) till March 31, 2024 to meet the increasing refinancing requirements. The leverage is expected to remain within this limit in the near term.

Nonetheless, SIDBI's exposure to various banks attracts a low risk weight of 20%, resulting in strong capital adequacy levels with a CRAR of 19.29% as on March 31, 2023, although the same moderated from 24.28% (entirely Tier I) as on March 31, 2022 (27.49% as on March 31, 2021) led by strong growth. ICRA notes that while the implementation of Basel III for AIFIs is yet to be announced, the eventual change in the method of computing risk-weighted assets upon the adoption of Basel III will not impact the capital metrics materially. Therefore, the overall capitalisation profile is expected to remain strong.

Credit challenges

Growth linked to availability of low-cost MSE fund allocations/RIDF deposits and refinance demand – SIDBI's growth prospects remain linked to the extent of coverage achieved by SCBs in meeting their PSL targets. As SCBs progressively achieve higher PSL targets, the overall allocation under MSE funds could drop, thereby affecting the growth prospects in the long term. Moreover, the MSE fund allocation of Rs. 3.33 lakh crore for FY2018-24 has, to a major extent, supported SIDBI's overall growth. Additionally, PSL shortfalls are allocated to other eligible AIFIs like National Housing Bank (NHB) and National Bank for Agriculture and Rural Development (NABARD) apart from Micro Units Development & Refinance Agency Ltd. (MUDRA). The annual allocation to SIDBI will also remain dependent on its relative importance compared to other AIFIs, which could result in lower allocations in case of increased allocation or preference to others.

Furthermore, as liquidity conditions tightened in FY2023, the demand for refinance grew sharply, which led to a steep increase in SIDBI's overall market borrowings. This, along with higher MSE Refinance allocations, supported the strong growth in net advances, which increased by ~76% YoY to Rs. 3.56 lakh crore as on March 31, 2023 from Rs. 2.02 lakh crore as on March 31, 2022. The overall growth momentum is likely to continue as systemic liquidity levels are expected to remain tight in the near term. This has resulted in higher leverage and a sustained growth in advances could lead to capital requirements next year.

Relatively concentrated exposure in indirect lending segment – SIDBI's lending is concentrated towards SCBs (84% as on March 31, 2023) followed by private sector entities (6%) and NBFCs (~9%). With a high share of refinancing to banks, the concentration of the top 20 borrowers in the total exposure remained high at ~68% as on March 31, 2023 (~61% as on March 31, 2022). This is, however, mitigated by the limited credit risk in the refinance portfolio of banks.

Modest earnings profile, mainly driven by fixed margins in refinance book – Given the cap on lending margins in the refinance business and the high share of MSE funds in overall liabilities, the earnings profile, in terms of the RoA, remains modest. The gross interest spread improved to 1.34% in FY2023 (1.02% in FY2022) while the net interest margin (NIM/Average total assets) witnessed a relative improvement to 1.71% in FY2023 from 1.37% in FY2022, leading to a higher operating profitability level (1.60% in FY2023 against 1.21% in FY2022). The improvement in the profitability was driven by the higher average loan book throughout the year. Due to lower slippages, the credit cost remained in check at 0.26% in FY2023 but was mildly higher than the previous year's level (0.16% in FY2022), given the increase in the standard asset provisions. As a result, the earnings profile improved with an RoA and RoE of 1.03% and 12.02%, respectively, in FY2023 (0.89% and 7.96%, respectively, in FY2022). Going forward, any regulatory change regarding the lending margins will remain a key monitorable for SIDBI's profitability.

Liquidity position: Superior

As a large part of SIDBI's loan book comprises refinance with a three-year tenure, which is largely funded through MSE Refinance deposits and long-term borrowings of a similar maturity, the overall asset and liability management (ALM) profile remains well matched to a large extent. As a result, SIDBI had positive cumulative asset-liability gaps across all maturity buckets as on March 31, 2023. Further, it had undrawn lines of ~Rs. 3,925 crore from banks and MSE Refinance allocations of ~Rs. 75,000 crore as on June 30, 2023, which can be called on short notice and drawn to meet any shortfall/funding gaps in future.

Rating sensitivities

Positive factors – Not applicable

Negative factors – ICRA could assign a Negative outlook or downgrade the rating in case of a dilution in SIDBI's strategic role and importance to the GoI.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA Rating Methodology for Banks and Financial Institutions Impact of Parent or Group Support on Issuer Credit Rating ICRA's Policy on Withdrawal of Credit Ratings Rating Approach – Consolidation
Parent/Group support	ICRA expects SIDBI to remain important to the GoI for supporting the growth of the MSME sector in India and expects the GoI to provide financial support, including MSE fund allocation and capital, if required
Consolidation/Standalone	For arriving at the rating, ICRA has considered the standalone financials of SIDBI. However, in line with its limited consolidation approach, ICRA has factored in the capital requirement of SIDBI's subsidiaries. In ICRA's view, the subsidiaries will remain self-sufficient in meeting their capital requirements in the near to medium term

About the company

Small Industries Development Bank of India (SIDBI) is an FI, constituted under an Act of Parliament (SIDBI Act, 1989), for the promotion and development of the MSME sector in India. SIDBI is jointly owned by the GoI (largest shareholder with a stake of 20.85% as on March 31, 2023), SBI (15.65%), LIC (13.33%) and other PSBs (the balance). ICRA notes that the GoI directly controls the operations of all the shareholders of SIDBI, which indirectly gives it total access to the entity's operations.

SIDBI's board of directors consists of –

- The Chairman & Managing Director appointed by the Central Government (for a term of 3 years)
- Two whole-time directors appointed by the Central Government
- Two directors who shall be officials of the Central Government
- Three directors to be nominated in the prescribed manner by the development bank, the PSBs, General Insurance Corporation of India (GIC), LIC and other institutions owned or controlled by the Central Government
- Three directors, including one from the officials of the state financial corporations, nominated by the Central Government from among persons with special knowledge of or professional experience in science, technology, economics, industry, banking, industrial cooperatives, law, industrial finance, investment, accountancy, marketing or any other matter
- Such number of directors, not exceeding four, elected in the prescribed manner by shareholders other than the development bank, the PSBs, GIC, LIC and other institutions owned or controlled by the Central Government

Key financial indicators (standalone)

	FY2021	FY2022	FY2023	Q1 FY2024
Net interest income	3,679	3,012	5,548	1,743
Profit after tax	2,398	1,958	3,344	792
Net advances (Rs. lakh crore)	1.56	2.02	3.56	3.65
Total assets (Rs. lakh crore)	1.92	2.47	4.02	NA
NIM/ATA	1.94%	1.37%	1.71%	NA
RoA	1.26%	0.89%	1.03%	NA
RoE	11.27%	7.96%	12.02%	11.20%
Tier I	27.49%	24.26%	18.81%	NA
CRAR	27.49%	24.28%	19.29%	15.63%*
Gross NPA	0.18%	0.11%	0.01%	0.02%
Net NPA	0.12%	0.07%	0.00%	0.01%
PCR (excl write-offs)	34.49%	39.34%	74.33%	42.86%

*Source: SIDBI & ICRA Research; Amount in Rs. crore unless mentioned otherwise; All ratios as per ICRA's calculations; * CRAR, as on June 30, 2023, does not include profits for the first quarter; if included, the CRAR stood at 18.5%*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

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 17, 2022	Mar 17, 2022	Feb 22, 2022	Jan 10, 2022	Jan 13, 2021
1	Long-term bonds programme	Long term	38,015.00*	36,805.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-	-	-
2	Long-term bonds programme	Long term	620.00	-	[ICRA]AAA (Stable); withdrawn	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)

Source: ICRA Research

**Balance yet to be placed/to be placed – Rs. 1,210.00 crore as on August 11, 2023*

Complexity level of the rated instrument

Instrument	Complexity Indicator
Long-term 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 instruments 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
INE556F08JP6	**Long-term bonds**	Feb-27-2020	6.27%	Feb-27-2023	620.00	[ICRA]AAA (Stable); withdrawn
INE556F08JQ4	**Long-term bonds**	Aug-18-2020	4.90%	Aug-18-2023	500.00	[ICRA]AAA (Stable)
INE556F08JR2	**Long-term bonds**	Dec-17-2020	4.58%	Dec-18-2023	250.00	[ICRA]AAA (Stable)
INE556F08JV4	**Long-term bonds**	Mar-02-2022	5.57%	Mar-03-2025	2,500.00	[ICRA]AAA (Stable)
INE556F08JW2	**Long-term bonds**	Mar-16-2022	5.40%	Mar-17-2025	1,525.00	[ICRA]AAA (Stable)
INE556F08JX0	**Long-term bonds**	Mar-28-2022	5.70%	Mar-28-2025	1,625.00	[ICRA]AAA (Stable)
INE556F08JY8	**Long-term bonds**	May-31-2022	7.15%	Jun-2-2025	2,500.00	[ICRA]AAA (Stable)
INE556F08JZ5	**Long-term bonds**	Jul-18-2022	7.15%	Jul-21-2025	3,000.00	[ICRA]AAA (Stable)
INE556F08KA6	**Long-term bonds**	Jul-28-2022	7.25%	Jul-31-2025	3,905.00	[ICRA]AAA (Stable)
INE556F08KB4	**Long-term bonds**	Aug-17-2022	7.11%	Feb-27-2026	4,000.00	[ICRA]AAA (Stable)
INE556F08KC2	**Long-term bonds**	Sep-08-2022	7.23%	Mar-09-2026	4,000.00	[ICRA]AAA (Stable)
INE556F08KD0	**Long-term bonds**	Oct-14-2022	7.75%	Oct-27-2025	4,000.00	[ICRA]AAA (Stable)
INE556F08KE8	**Long-term bonds**	Nov-15-2022	7.47%	Nov-25-2025	4,000.00	[ICRA]AAA (Stable)
INE556F08KF5	**Long-term bonds**	Dec-02-2022	7.54%	Jan-12-2026	5,000.00	[ICRA]AAA (Stable)
Unplaced	**Long-term bonds**	Unutilised	NA	NA	1,210.00	[ICRA]AAA (Stable)

Source: Company

Annexure II: List of entities considered for consolidated analysis

Name of the Entity	Ownership	Consolidation Approach
MUDRA Ltd.	100.0%	Limited Consolidation
SIDBI Venture Capital Ltd (SVCL)	100.0%	Limited Consolidation
SIDBI Trustee Company Ltd	100.0%	Limited Consolidation

Source: SIDBI and ICRA Research

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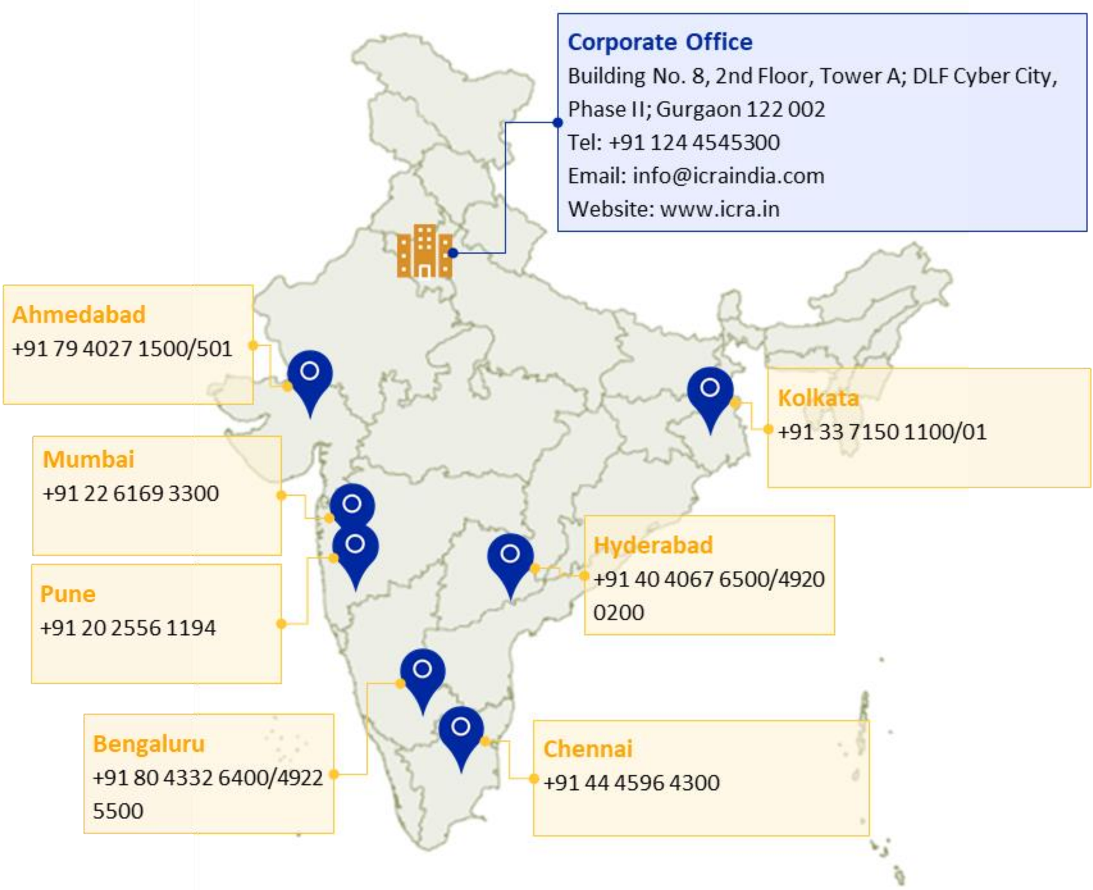

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