October 19, 2023(Revised)

Bandhan Bank Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
NCD programme	75.00	75.00	[ICRA]AA (Negative); reaffirmed
NCD programme	35.00	-	[ICRA]AA (Negative); reaffirmed and withdrawn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
Total	**3,190.00**	**3,155.00**	

**Instrument details are provided in Annexure I*

Rationale

The ratings reaffirmation continues to factor in Bandhan Bank Limited's (Bandhan) strong capitalisation levels with a Tier I capital ratio of 19.45% as on June 30, 2023. Bandhan also benefits from its strong liquidity profile, supported by its increasing deposit base, high share of retail deposits and priority sector loan (PSL) book.

The Negative outlook reflects continued weakness in the asset quality profile, with high fresh slippage rate of 7.5% (annualised) of standard advances in Q1 FY2024 (10.5% in FY2023), majorly from the emerging entrepreneur business (EEB) segment. This has also resulted in elevated credit provisions because of which the profitability of the bank continues to be below the pre-pandemic levels.

While the 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) + SMA[1] 1 + SMA 2) remained elevated at 12.2% of the EEB portfolio as on June 30, 2023. Including the non-EEB portfolio, the gross stressed book stood at 8.2% of gross advances as on June 30, 2023. The bank has steadily increased the provision on its stressed book and, net of provisions, the net stressed book stood at 3.8% of net advances as on June 30, 2023. Though the net stress book has moderated, however, the sufficiency of provisions will be dependent on timely receipt of claims against these stressed loans under various schemes of the Government. In an event of any delay in recoveries, the provisioning could lead to net stressed assets and profitability remaining weaker, the negative trigger.

ICRA has withdrawn the rating assigned to the Rs. 35.0 crore of NCD programme as these have been fully redeemed and no amount is outstanding against the same. The rating was withdrawn in accordance with ICRA's policy on the withdrawal of credit ratings (click here for the policy).

Key rating drivers and their description

Credit strengths

Long track record in micro-finance loan segment – 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

[1] 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.

of borrowers and, hence, the asset quality of the bank. While Bandhan has diversified into secured lending through its merger with GRUH Finance Limited in FY2020, microloans (or EEB segment) continued to account for 50% of its loan portfolio as on June 30, 2023.

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 PSL eligible loans, the NOI from the sale of PSLCs has significantly declined. As a result of this, the bank had to place the shortfall from past PSLC sales in low-yielding RIDF deposits, which will continue to be a drag on the profitability of the bank in the near term. Given its presence in the microloan segment, the operating profitability remains strong; nevertheless, a marginal borrower profile, makes the portfolio vulnerable to any episodic events, that may translate into higher credit costs.

Strong capital position; ability to meet targeted recovery from stressed pool remains monitorable – The bank's capitalisation profile continues to be strong with the Tier I ratio of 19.45% and capital-to-risk weighted assets ratio (CRAR) of 20.45% as on June 30, 2023 (Tier I 18.30% and CRAR 19.40 as on June 2022 and Tier I ~23.85% and CRAR ~24.81% as on June 2021). The capitalisation metrics have been on a declining trajectory because of increase in risk weighted assets (RWA) on account of loan book growth amid moderation in profitability from past levels. The bank last raised equity capital of Rs. 3,662 crore in FY2018 as part of its initial public offering (IPO) and since then, its capital position has largely been supported by internal accruals.

Bandhan's ability to grow while maintaining and improving its capitalisation profile would remain contingent upon the restoration of its profitability, which will remain a function of lower credit costs. Incrementally, credit cost will also be dependent on timely receipt of claims against these stressed loans under various schemes of the Government (ECLGS[2], CGFMU[3] and AMFIRS[4]). While the bank expects credit provisions to remain at 2.0-2.5% of advances in FY2024, which is lower than very high annualised credit cost of 6.39% during FY2021-FY2023, however this will be contingent on timely recoveries from borrowers or the Government schemes.

Healthy growth in deposits with higher share of retail deposits – The overall deposit base expanded by 16.6% Year-on-Year (YoY) to Rs. 1,08,480 crore as on June 30, 2023. The share of retail deposits in total deposits was 71% in June 2023, though it has moderated from 78% in June 2022. The share of CASA deposits in total deposits also declined to 36% in June 2023 from 43.2 % in June 2022, as depositors continue to shift to term deposits amid rising deposit rates. The deposit growth is also supported by higher interest rate proposition on deposits (including saving deposits), which leads to a higher cost of interest-bearing fund of 6.25% in Q1 FY2024 compared to 4.95% for private sector bank average.

Credit challenges

Asset quality remains a monitorable, given the presence in marginal borrower profile segment – With a significant presence in the unsecured micro-banking segment, the asset quality has been impacted by the pandemic. While the asset quality at the industry level has seen an improvement, the fresh NPA generation rate remains elevated for the bank at 7.50% (annualised) in Q1 FY2024 (10.46% in FY2023 and 11.97% in FY2022). The GNPA moderated to 6.76% as on June 2023 from 7.16% as on June 2022, due to significant write offs and the net non-performing advances (NNPA) inched up to 2.18% as on June 2023 from 1.86% as on June 2022 with continued fresh slippages.

Overall, the stressed pool in the EEB segment was high at Rs. 6,238 crore or 12.2% of the EEB portfolio as on June 30, 2023, and the gross stressed pool (inclusive of the non-EEB book) stood at Rs. 8,448 crore or 8.2% of gross advances as on June 30, 2023. Net of the provisions, the net stressed book at the bank level stood at Rs. 3,628 crore or 3.8% of standard advances or 18.4% of the Tier I capital as on June 30, 2023. This has however improved from 16.6% of standard advances and 84.2% of Tier I capital as on September 30, 2021, driven by recoveries as well as provisions from operating profits. Despite the reduction in the net stress book of the bank, asset quality remains monitorable because of higher slippage rate, marginal profile of the

[2] ECLGS : Emergency credit guarantee scheme
[3] CGFMU: Credit Guarantee Fund for Micro Units
[4] AMFIRS: Assam Microfinance Incentive and Relief Scheme

borrowers and portfolio vulnerable to episodic events that may translate into higher credit costs. The bank's ability to contain slippages in the EEB segment and ensure timely recoveries from the stress pool will be a key credit monitorable.

High geographical concentration of loan portfolio – While Bandhan has increased its pan-India presence across 34 states and Union Territories (UTs), 56% of the banking outlets were in the eastern and north-eastern regions as on June 30, 2023. 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/overdue book, given the meaningful share of the state in overall advances. Following the merger with GRUH, the bank has diversified geographically, 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 any 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

Bandhan's largely stable deposit profile, coupled with the short tenure of microloans, largely supports its strong liquidity profile. The daily average liquidity coverage ratio (LCR) remained strong at 182.8% for Q1 FY2024, while the net stable funding ratio (NSFR) stood at 144.2%, with both remaining above the regulatory level of 100%. Additionally, it reported a sizeable cash and bank balance of Rs. 7,603 crore or 5.0% of the total assets as on June 30, 2023. 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 – A reduction in the net stressed assets portfolio (NPA + SMA1 + SMA2) to less than 3% of advances, improvement in its profitability with a return on assets (RoA) of >2.5% and maintaining the Tier I capital position above 20% on a sustainable basis, will be positive triggers.

Negative factors – An increase in the net stressed book (NPA + SMA1 + SMA2) to >5%, leading to continued uncertainty on the asset quality, capital and profitability or a decline in the Tier I ratio below 15% will be negative rating triggers.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA Rating Methodology for Banks and Financial Institutions ICRA's Policy on Withdrawal of Credit Rating
Parent/Group support	Not Applicable
Consolidation/Standalone	The ratings are based on the standalone financials of Bandhan

About the company

The 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%), Northeast Financial Inclusion Trust (NEFIT; 7.82%), and other 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, 2023, Bandhan had a network of 6,140 branches, banking units or doorstep service centres (DSCs) and GRUH centres, spread across 34 states and UTs.

Key financial indicators (audited)

Bandhan Bank	FY2022	FY2023	Q1 FY2023	Q1 FY2024
Net interest income	8,714	9,260	2,514	2,491
Profit before tax	129	2,893	1,178	960
Profit after tax	126	2,195	887	721
Net advances	93,975	1,04,757	90,883	98,197
Total assets	1,38,867	1,55,770	1,41,235	1,50,781
CET I/Tier I	18.90%	18.70%	18.30%	19.45%*
CRAR	20.10%	19.80%	19.40%	20.45%*
Net interest margin	6.87%	6.69%	7.18%	6.50%
PAT/ATA	0.10%	1.58%	2.53%	1.88%
Return on net worth	0.72%	12.52%	19.89%	14.46%
Gross NPAs	6.46%	4.87%	7.25%	6.76%
Net NPAs	1.66%	1.17%	1.92%	2.18%
Provision coverage excl. technical write-offs	75.48%	76.82%	74.90%	69.25%
Net NPA/Core equity capital	9.13%	6.46%	9.70%	10.84%*

Note: Amounts 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
**Including Q1 FY2024 profits.*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021	
					Oct 19,2023	Oct 28, 2022	Nov 9, 2021	Feb 24, 2021	Aug 10, 2020
1	Term loans*	LT	80.00	Nil	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
2	Certificates of deposit	ST	3,000.00	885.00^	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
3	Non-convertible debenture programme	LT	75.00	75.00	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
4	Non-convertible debenture programme	LT	35.00	-	[ICRA]AA (Negative); reaffirmed and withdrawn	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
4	Non-convertible debenture programme	LT	-	-	-	[ICRA]AA (Negative); reaffirmed and withdrawn	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
5	Non-convertible debenture programme	LT	-	-	-	-	-	[ICRA]AA (Stable); reaffirmed and withdrawn	[ICRA]AA (Stable)
6	Subordinated Tier II NCD	LT	-	-	-	-	[ICRA]AA (Negative); reaffirmed and withdrawn	[ICRA]AA (Stable)	[ICRA]AA (Stable)

**The amount is yet to be allocated*
^ Data as on October 11, 2023
LT – Long term; ST – Short term

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: Click Here

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	80.00	[ICRA]AA (Negative)
INE580B07455	**Non-convertible debentures^**	Oct-30-2018	9.50%	Oct-30-2028	75.00	[ICRA]AA (Negative)
INE545U16434	**Certificates of deposit**	Sep-08-2023	7.95%	Sep-09-2024	560.00	[ICRA]A1+
INE545U16442	**Certificates of deposit**	Sep-14-2023	7.95%	Sep-13-2024	175.00	[ICRA]A1+
INE545U16442	**Certificates of deposit**	Sep-22-2023	7.95%	Sep-13-2024	150.00	[ICRA]A1+
NA	**Certificates of deposit#**	NA	NA	7-365 days	2,115.00	[ICRA]A1+
INE580B07489	**Non-convertible debentures^**	Dec-06-2018	9.35%	Oct-31-2023	35.00	[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. # As on October 11, 2023

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

Corrigendum

Rationale dated October 19, 2023, has been revised with changes as below:

Reason for withdrawal of ratings has been updated in the rationale para on Page no.1.

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