

March 28, 2024

SBI DFHI Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer rating	-	-	[ICRA]AAA (Stable); reaffirmed
Commercial paper programme	950	950	[ICRA]A1+; reaffirmed
Total	950	950	

*Instrument details are provided in Annexure I

Rationale

The ratings factor in the strength of SBI DFHI Limited's parent, State Bank of India (SBI; rated [ICRA]AAA (Stable) for its Basel III Tier II bonds), which holds a 69.04% stake (total stake of 72.17% held by SBI Group) in the company. The ratings also consider the continued managerial, operational and financial support expected from SBI, given the shared brand name. The ratings reaffirmation also factors in SBI DFHI's adequate risk management policies and adherence to internal prudential norms, which mitigate the market risks associated with dealing in debt securities. The ratings also consider the company's strong capitalisation and sound asset profile. Given its healthy net worth base, the company has sufficient cushion to withstand the impact of adverse market movements, resulting in a strong capitalisation profile.

The ratings are supported by SBI DFHI's strong liquidity profile, as reflected in the high share of liquid Government securities (G-Secs) in the overall assets and access to call money and borrowings under repo from the market, apart from access to a standing liquidity facility (SLF) from the Reserve Bank of India (RBI) for participating in primary auctions. The share of non-statutory liquidity ratio (non-SLR) securities has remained higher than peers, but largely remains in highly rated corporate bonds and short-term money market instruments.

ICRA notes the susceptibility of the company's overall profitability and capitalisation profile to interest rate movements, given the nature of its business and the high share of debt securities in the overall assets. Additionally, it has kept its leverage high in the past few quarters to maintain its net interest income (NII) amid the rise in short-term borrowing costs and the limited term premium across various debt maturities, which increases its vulnerability to market risks. This is also reflected in the trading losses witnessed during FY2022-FY2023 amid the rising interest rates. Meanwhile, SBI DFHI's NII has moderated on account of the increase in short-term borrowing costs after the hikes in the monetary policy rates and the tight liquidity environment in H2 FY2024.

As policy rates have peaked and could witness a shallow cut in H2 FY2025, the short-term rates are unlikely to see a material increase from the current levels. Additionally, the NII level could improve while the interest rate environment could remain conducive for increased trading opportunities in the near to medium term. While SBI DFHI's income remains less diverse and its earnings profile remains susceptible to adverse interest rate movements, its ability to adhere to its risk management policies, will remain critical for the overall profitability. Continued linkages with the parent and the ability to withstand interest rate cycles and any regulatory changes for primary dealers (PDs) will remain key rating sensitivities. Nevertheless, the company's strong capitalisation profile provides comfort. The ratings will remain sensitive to SBI's shareholding and its continued support to the company.

Key rating drivers and their description

Credit strengths

Strong parentage – ICRA takes comfort from the strong parentage in the form of SBI (69.04% stake as on December 31, 2023), the shared brand name and the resulting operational, managerial and financial support from the SBI Group. The company's board of directors consists of members who had previously served at SBI. Further, its key management personal are on deputation from the bank. SBI has also sanctioned bank lines of Rs. 2,750 crore, including an intraday facility, as funding support to SBI DFHI. In ICRA's view, the company is likely to continue receiving support, if required. Nevertheless, the ratings will remain sensitive to SBI's shareholding in SBI DFHI and its continued support to the company.

Strong capitalisation profile – SBI DFHI's capital adequacy remains strong with its capital-to-risk weighted assets ratio (CRAR) at 34.30% as on December 31, 2023 (46.17% as of March 2023 and 30.96% as of December 2023), well above the minimum regulatory requirement of 15% for PDs. The daily average leverage increased to 14.47 times in 9M FY2024 (10.93 times in FY2023) to maintain the NII amid the rising short-term funding rates and limited term premium on debt securities.

As it is a PD, the underwriting and trading of G-Secs constitute the company's core activity. Therefore, its profitability and capital profile are susceptible to market risks arising out of interest rate movements. Given the vulnerability of trading volumes and profitability to market volatility, a PD's net worth assumes considerable significance from a credit perspective. SBI DFHI's net worth of Rs. 1,557 crore (net owned funds (NOF) of Rs. 1,367¹ crore), as on December 31, 2023, provides considerable comfort. The price value of a basis point (PVBP²) stood at Rs. 2.92 crore as on December 31, 2023, indicating adequate ability to absorb large adverse movements in interest rates while maintaining the CRAR above the regulatory requirement.

Sound asset profile – SBI DFHI maintains 76.1% of its total assets in the form of SLR investments (non-SLR portfolio stood at Rs. 3,789 crore or 5.0% of total assets as on December 31, 2023). Credit risk largely emanates from the non-SLR portfolio and the company had only one non-performing investment of Rs. 45.99 crore as of March 31, 2021, which was partly recovered in FY2022 while the balance was written off. Apart from this, there were no credit losses in the past six years and the net non-performing assets (NPA) remained nil as on December 31, 2023.

Strong liquidity profile – The company has a large portfolio of highly liquid G-Secs {Central/state government and Government of India (GoI) Treasury bills (T-bills)}. On a daily average basis, investment in G-Secs comprised ~81% of the total assets in 9M FY2024 (~78% in FY2023). Other assets include investments in highly rated corporate bonds. SBI DFHI's non-SLR or corporate debt investment portfolio has also remained well diversified across highly rated corporates. About 30% of the non-SLR book was in short-term money market instruments while 70% was in AAA/AA rated corporates as of December 31, 2023. Corporate debt investments can be funded through term and call/notice (subject to daily average of 50% of NOF), commercial paper, inter-corporate deposits (150% of NOF) or bank lines. These investments can also be sold off to generate liquidity if required. With funds parked in highly liquid investments, SBI DFHI's overall liquidity remains strong.

SBI DFHI's liquidity is also supported by its access to the money market for call and repo borrowings, apart from the sanctioned bank limits of Rs. 2,750 crore from SBI (including intraday facility of Rs. 1,100 crore, overnight/term facility of Rs. 1,550 crore and Rs. 100-crore lines of credit) and the Rs. 900-crore intraday line from other banks. Though SBI DFHI's liabilities are largely short term in nature compared to the long tenure of its assets, the liquid nature of the assets mitigates the asset-liability risk.

Adequate internal prudential norms and risk management systems – Prudent risk management policies and adherence to the same are critical for a PD, given its susceptibility to market risk related to debt securities and credit risk on account of non-SLR securities. ICRA takes comfort from the adequate risk management policies approved by the company's Risk Management Committee, comprising members from the board, with well-defined limits for various exposures and loss mitigation measures.

¹ SBI DFHI has investments in The Clearing Corporation of India Limited (rated [ICRA]AAA (Stable)/[ICRA]A1+), which is knocked off from the net worth, resulting in lower NOF compared to the net worth

² PVBP measures the gain/loss on the entire portfolio for a 1 bps (0.01%) movement in the interest rate

The Committee also monitors and ensures adherence to these policies on a daily basis. As per the risk management policy, investment in non-SLR securities is allowed only for investment with a minimum rating of AA- for the private sector and A- for public sector undertakings, mitigating the credit risk to a certain extent. However, in practice, the company does not invest in securities with a rating below AAA/AA. Entities rated AAA/A1+ accounted for ~93% of the total non-SLR portfolio by value as on December 31, 2023.

Credit challenges

Low diversification of revenues – SBI DFHI's revenue stream is relatively less diversified compared to other PDs, with interest income and trading income accounting for almost 100% of its total revenue. The company earned underwriting and other income of Rs. 5 crore in 9M FY2024 (Rs. 5 crore in FY2023 and Rs. 16 crore in FY2022). Other income in 9M FY2024 and FY2023 declined from the FY2022 level on account of the favourable demand for G-Secs as reflected in the lower devolvement of G-Secs on PDs, leading to lower underwriting fees charged by PDs. Going forward, the revenue and profitability will remain linked to the quantum of government borrowing as well as the extent of underwriting commission.

Earnings vulnerable to interest rate movements – As the company's portfolio largely comprises debt securities, its earnings profile remains susceptible to adverse movements in the interest rates. This is reflected in the sizeable variation in trading income (including mark-to-market (MTM) gains/losses) during the past few fiscals because of the movement in bond yields (trading profit of Rs. 70 crore in 9M FY2024 against trading losses of Rs. 125 crore in FY2023 and Rs. 101 crore in FY2022). Additionally, as short-term interest rates began to rise sharply in FY2023, the net interest margin narrowed to 0.77% in 9M FY2024 from 1.24% in FY2023 and 2.75% in FY2022 due to the higher cost of funds. This resulted in a decline in the profit to Rs. 20 crore in FY2023 from Rs. 142 crore in FY2022 and Rs. 252 crore in FY2021. With the increased size of the investment portfolio and the favourable movement in bond yields, the net profit improved to Rs. 119 crore in 9M FY2024 compared to the net loss of Rs. 17 crore in 9M FY2023.

Vulnerability to changes in regulatory framework for PDs – The RBI is the regulatory authority for PDs and has prescribed operational guidelines for underwriting commitments for G-Secs, bidding commitments and success ratios for T-bills, the achievement of minimum turnover ratios and funding support in the form of the SLF. Therefore, any significant change in the regulatory framework for PDs, which adversely impacts the company's operational and financial profile, can affect its funding costs and profitability.

Liquidity position: Strong

The company has a strong liquidity profile, given the inherent nature of the PD business. This is demonstrated by the high share of G-Secs in the total assets (78% of total assets on a daily average basis for 9M FY2024). Furthermore, SBI DFHI's non-SLR book (19% of investments on a daily average basis for 9M FY2024) largely comprises highly rated corporate debt securities, thereby minimising the liquidity risk in the corporate bond portfolio to a certain extent. The liquidity is also supported by the company's access to the money market for call and repo borrowings, in addition to the RBI's SLF funding, apart from bank limits.

Rating sensitivities

Positive factors – Not applicable

Negative factors – A deterioration in SBI's credit profile can lead to a rating downgrade. Additionally, a significant change in the shareholding or linkages with SBI DFHI will be a negative factor. Sustained losses, which result in considerable erosion of the net worth, or any regulatory change adversely impacting the PD business will also remain negative factors.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology for Primary Dealers Implicit parent or group support
Parent/Group support	ICRA expects SBI to provide financial, managerial and operational support when required, given the shared brand name and SBI's ownership
Consolidation/Standalone	To arrive at the ratings, ICRA has considered the standalone financials of the company

About the company

SBI DFHI is a State Bank of India Group Company, created from the merger of the RBI-promoted Discount & Finance House of India (DFHI) and SBI Gilts Limited (subsidiary of SBI) in 2004. SBI DFHI was incorporated under the provisions of the Companies Act, 1956 (as amended by the Companies Act, 2013) on March 8, 1988. It is registered as a non-banking financial company (NBFC) and is a standalone PD created to support the book building process for the primary auction of G-Secs. Its shareholders include scheduled commercial banks (public and private sector banks), including SBI, insurance companies and All India Financial Institutions.

SBI DFHI is one of the largest standalone PDs in the country in terms of net worth (Rs. 1,557 crore as on December 31, 2023). It reported a net profit of Rs. 119 crore (annualised RoA of 0.90% and return on equity (RoE) of 10.21%) on total income of Rs. 1,088 crore in 9M FY2024 compared to a net profit of Rs. 20 crore (RoA of 0.13% and RoE of 1.45%) on total income of Rs. 856 crore in FY2023.

Key financial indicators

SBI DFHI Limited	FY2022	FY2023	9M FY2024*
Profit after tax (PAT)	142	20	119
Net worth	1,452	1,394	1,557^
Total assets	13,079	17,267	22,286
PAT/Net worth (RoNW)	9.78%	1.45%	10.21%#
Leverage ratio (daily average; times)	8.20	10.93	14.47

Source: SBI DFHI, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations; Amount in Rs. crore; #Annualised

^ Including other comprehensive Income (OCI) of Rs. 45 crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Type	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years		
			Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2024		Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					Mar 28, 2024	Apr 28, 2023			
1	Issuer rating	Long term	-	-	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
2	Commercial paper programme	Short term	950	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Issuer rating	Not Applicable
Commercial paper programme	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	Issuer rating	NA	NA	NA	-	[ICRA]AAA (Stable)
Not placed	Commercial paper programme	NA	NA	NA	950	[ICRA]A1+

Source: Company

Annexure II: List of entities considered for consolidated analysis

Not applicable

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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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Branches



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