March 25, 2025

Dhanlaxmi Bank Limited: [ICRA]BBB- (Stable) assigned to Basel III Tier II bonds

Summary of rating action

Instrument*	Current rated amount (Rs. crore)	Rating action
Basel III Tier II bonds	150.00	[ICRA]BBB- (Stable); assigned
Total	**150.00**	

**Instrument details are provided in Annexure I*

Rationale

The rating factors in Dhanlaxmi Bank Limited long-standing track record of over 97 years in the banking sector and its established presence in South India, especially in Kerala. While the bank has reported low capital cushions in the past due to weak internal accruals, it raised Rs. 297.5 crore in February 2025 via a rights issue, which has helped improve its capitalisation and solvency profile. ICRA expects the growth prospects to improve due to the fresh capital raise.

Dhanlaxmi's profitability has remained weak over the past several years due to the relatively low net interest margin (NIM) and high operating expenses, which kept its capital buffers low, impacting its ability to grow its loan book. Loan book growth picked up at a healthy pace for a year or two after the bank exited the prompt corrective action (PCA) framework in February 2019. However, the overall growth has been moderate since then. Hence, the scale of operation remains small. The bank's net advances declined to Rs. 6,289 crore as on March 31, 2019 from Rs. 9,065 crore as on March 31, 2011 due to advisory/restrictions under the Monitorable Action Plan (MAP) and the PCA, resulting in a decline in its market share. Net advances reached Rs. 11,069 crore as on December 31, 2024, increasing at a compound annual growth rate (CAGR) of 10.0% during March 2019-December 2024.

While the bank's fresh non-performing advances (NPA) generation rate has moderated and the headline asset quality metrics have improved over the years, the same remains monitorable, especially given the increasing stress in the retail segment. Dhanlaxmi's ability to absorb credit costs due to asset quality shocks remains constrained by its weak operating profitability. Additionally, the bank's top 20 exposures remain concentrated in relation to its capital while the liability base also continues to be concentrated with the top 20 depositors forming 22.3% of total deposits as on March 31, 2024. ICRA, however, notes that a sizeable share of the deposits from the top depositor is non-callable, reducing the liquidity risk to an extent.

ICRA also takes note of the presence of two Reserve Bank of India (RBI) appointed directors on Dhanlaxmi's board.

Key rating drivers and their description

Credit strengths

Long-standing track record and established presence in South India – Dhanlaxmi has an operational track record of more than 97 years and has established a retail franchise in southern India. It had a network of 261 branches as on December 31, 2024, with more than 80% in the southern states of Tamil Nadu, Andhra Pradesh, Telangana, Kerala and Karnataka. The bank has a healthy share of retail deposits, which support its overall liquidity profile. ICRA also notes that a sizeable share of the deposits from the top depositor is non-callable, reducing the liquidity risk to an extent.

Capitalisation profile improves after rights issue – The bank reported a Tier I capital ratio and a capital-to-risk weighted assets ratio (CRAR) of 11.8% (Rs. 880.0 crore) and 12.8% crore (Rs. 950.5 crore), respectively, as on December 31, 2024. While it has reported low capital cushions in the past due to weak profitability and delay in raising capital, the fresh capital raise of Rs. 297.5 crore in February 2025 via a rights issue has helped improve its capital position. The fresh capital infusion will provide Dhanlaxmi with the requisite growth capital. ICRA expects the bank's internal accruals to remain modest in the near to medium term. Thus, its ability to meaningfully improve its market position will depend on the raising of fresh capital in the future.

Credit challenges

Weak profitability – While Dhanlaxmi has remained profitable since FY2019, its profitability metrics continue to be weak. Apart from high operating costs, the relatively lower NIMs are due to the suboptimal credit-to-deposit ratio as well as the yield on assets. The bank's net credit-to-deposit ratio stood at 73.5% as on December 31, 2024 (70.7% as on March 31, 2024) compared to 91% for private sector banks as on December 31, 2024, resulting in lower net interest income of 2.86% in 9M FY2025 as a percentage of average total assets (2.96% in FY2024). Moreover, it reported an operating cost to operating income ratio of 88.1% in 9M FY2025 (88.7% in FY2024), leading to a weak return on assets (RoA) of 0.31% (0.38% in FY2024). The bank's ability to bring down the operating cost to income ratio will be driven by its ability to scale up the assets while containing slippages. This would remain critical from a profitability perspective.

Small scale of operations and modest growth – Dhanlaxmi has a small scale of operations with a net loan book of Rs. 11,069 crore as on December 31, 2024, translating into a loan book market share of 0.1%. It has witnessed limited growth in its balance sheet over the years due to advisory/restrictions under MAP (CY2011-CY2014) and PCA (CY2014-CY2019), resulting in a decline in the loan book during this period to Rs. 6,289 crore as on March 31, 2019 from Rs. 9,065 crore as on March 31, 2011. After exiting the PCA framework in February 2019, Dhanlaxmi witnessed modest loan book growth due to weak internal accruals and delay in raising capital. Moreover, it has not been able to expand its branch network over the years due to restrictions by the regulator amid high operating costs. With the infusion of fresh capital in FY2025, ICRA expects the loan book growth to improve.

Asset quality remains monitorable – Dhanlaxmi reported a manageable fresh NPA generation rate of 1.48% in 11M FY2025 (1.63% in FY2024, 1.27% in FY2023). Moreover, the gross NPA (GNPA%) and net NPA (NNPA%) improved due to strong recoveries, upgrades, write-offs and loan book growth, standing at 3.53% and 0.86%, respectively, as on December 31, 2024 (4.05% and 1.25%, respectively, as on March 31, 2024). Nevertheless, the trend remains monitorable, especially given the increasing stress in the retail segment.

However, the bank's exposure remains concentrated with the top 20 exposures accounting for 14.40% of the total exposure (200% of Tier I capital) as on March 31, 2024. Additionally, the vulnerable book, consisting of SMA[1]-1 and 2 and the standard restructured book, was Rs. 155 crore (17.6% of Tier I capital) as on December 31, 2024. Given the weak operating profitability, Dhanlaxmi's ability to absorb increased credit costs remains limited.

Environmental and social risks

While banks like Dhanlaxmi do not face material physical climate risks, they are exposed to environmental risks indirectly through their portfolio of assets. If the entities or businesses, to which banks and financial institutions have an exposure, face business disruptions because of physical climate adversities or if such businesses face climate transition risks because of technological, regulatory or customer behaviour changes, it could translate into credit risks for banks. However, such risk is not material for Dhanlaxmi as it benefits from adequate portfolio diversification. Further, the lending is typically short-to-medium term, allowing it to adapt and take incremental exposure to businesses that face relatively fewer downside environmental risks.

[1] *SMA is defined as a special mention account (SMA), which is an account exhibiting signs of incipient stress resulting in the borrower defaulting in the timely servicing of their debt obligations though the account has not yet been classified as an NPA as per the extant RBI guidelines; SMA-1 accounts are overdue by 31-60 days while SMA-2 accounts are overdue by 61-90 days*

With regard to social risks, data security and customer privacy are among the key sources of vulnerability for banks as material lapses could be detrimental to their reputation and invite regulatory censure as has been seen for other regulated entities in the recent past. While Dhanlaxmi has not faced material lapses over the years, high operating expenses could limit its ability to invest in information technology (IT) infrastructure. While it contributes to promoting financial inclusion by lending to underserved segments, its lending practices remain prudent as reflected in the healthy asset quality numbers in this segment compared with its peers.

Liquidity position: Adequate

While the bank's daily average liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) of 148.2% and 148.8%, respectively, for Q3 FY2025, stand well above the regulatory requirement of 100%, liquidity remains constrained by the high concentration of depositors with the top 20 depositors accounting for 22.3% of the total deposits as on March 31, 2024. The liquidity position is supported by positive asset-liability mismatches (as per the structural liquidity statement as on December 31, 2024) in all the less-than-1-year maturity buckets. Dhanlaxmi can also avail liquidity support from the RBI (through repo against excess statutory liquidity ratio (SLR) investments and marginal standing facility mechanism) in case of urgent liquidity needs.

Rating sensitivities

Positive factors – ICRA could upgrade the rating if the bank is able to increase its scale of operations meaningfully while improving its profitability and maintaining adequate capital cushions over the regulatory levels on a sustained basis.

Negative factors – ICRA could downgrade the rating if there a weakening in the earnings profile and/or a decline in the capital cushions to less than 2% in relation to the Tier I or CRAR regulatory levels on a sustained basis.

Analytical approach

Analytical approach	Comments
Applicable rating methodologies	ICRA's Rating Methodology for Banks and Financial Institutions
Parent/Group support	Not applicable
Consolidation/Standalone	To arrive at the rating, ICRA has considered the standalone financials of Dhanlaxmi Bank. The bank does not have any subsidiaries.

About the company

Dhanalakshmi Bank Limited was incorporated on November 14, 1927 under the erstwhile Indian Companies Act, 1913. It became a scheduled commercial bank in 1977 under the Second Schedule of the RBI Act and its name was subsequently changed to Dhanlaxmi Bank Limited. The bank did not have any subsidiaries/associates as on December 31, 2024. It had a network of 261 branches and 282 ATMs, as on December 31, 2024, across India (mainly in South India).

Dhanlaxmi reported a net loan book of Rs. 11,069 crore and total assets of Rs. 16,634 crore as on December 31, 2024. It reported a net profit of Rs. 38 crore in 9M FY2025 (Rs. 58 crore in FY2024).

Key financial indicators (standalone)

Dhanlaxmi Bank	FY2023	FY2024	9M FY2025
Total income	550.27	611.01	475.17
Profit after tax	49.36	57.82	37.66
Total assets	15,132	15,962	16,634
CET I/Tier I	10.55%	11.36%	11.83%*
CRAR	12.32%	12.71%	12.79%*
PAT/ATA	0.34%	0.38%	0.31%^
Gross NPA	5.19%	4.05%	3.53%
Net NPA	1.16%	1.25%	0.86%

Source: Dhanlaxmi Bank, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore

Total income includes net interest income and other income
**Excluding interim period profits*
^Annualised

Status of non-cooperation with previous CRA: Brickwork Ratings placed Dhanlaxmi on issuer not co-operating category due to non-submission of a no-default statement (NDS), inadequate information and lack of management cooperation. Their latest press release (PR) is dated July 11, 2024.

Any other information: Not applicable

Rating history for past three years

Name of instrument	Current rating (FY2025)			Chronology of rating history for the past 3 years		
	Type	Amount rated (Rs. crore)	Date & rating in FY2025	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022
			March 25, 2025	-	-	-
Basel III Tier II bonds	Long term	150.00	**[ICRA]BBB- (Stable)**			

Complexity level of the rated instruments

Instrument	Complexity indicator
Basel III Tier II bonds	Highly Complex

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/ Sanction	Coupon rate	Maturity date	Amount rated (Rs. crore)	Current rating and outlook
Proposed/Not placed	**Basel III Tier II bonds**	-	-	-	150.00	[ICRA]BBB- (Stable)

Source: Dhanlaxmi, ICRA Research

Key features of the rated instrument

The servicing of the Basel III Tier II bonds is not subject to any capital ratios and profitability. However, these bonds are expected to absorb losses once the point of non-viability (PONV) trigger is invoked. Further, the exercise of the call option (if any) on the Basel III Tier II bonds is contingent upon the prior approval of the RBI and the bank will need to demonstrate that its capital position is well above the minimum regulatory requirement, following the exercise of the said call option.

Annexure II: List of entities considered for limited 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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