

May 22, 2025

Utkarsh Small Finance Bank Limited: Ratings reaffirmed and outlook revised to Negative

Summary of rating action

Instrument*	Previous rated amount (Rs. crore)	Current rated amount (Rs. crore)	Rating action
Subordinated debt	400.0	400.0	[ICRA]A+ (Negative); reaffirmed and outlook revised to Negative from Stable
Certificates of deposit	1,000.0	1,000.0	[ICRA]A1+; reaffirmed
Total	1,400.0	1,400.0	

*Instrument details are provided in Annexure I

Rationale

The revision in the outlook to Negative considers the significant deterioration in Utkarsh Small Finance Bank Limited's (Utkarsh) asset quality and earnings profile in FY2025 and the subdued performance expected in the near term. The bank's gross non-performing assets increased to 9.4% as of March 2025 from 2.5% as of March 2024 amid industry-wide stress in the asset quality of the microfinance portfolio. Consequently, the earnings profile was adversely impacted and the overall profitability was muted with Utkarsh reporting a net profit of Rs. 24 crore in FY2025 vis-à-vis Rs. 498 crore in FY2024.

The deterioration in the asset quality was primarily on account of higher slippages in the microfinance portfolio due to various factors including, but not limited to, overleveraging by borrowers, worsened credit discipline, adverse climatic conditions and other operational challenges like employee attrition. ICRA takes note of the corrective measures being taken by the bank. Although incremental inflow to the special mention account (SMA) bucket has slowed down, the near-term performance shall remain monitorable considering the tightened guardrails for the microfinance sector. Further, the asset quality in Utkarsh's relatively newer product segments remains monitorable, given the sizeable scaleup in the last 2-3 years.

Given the deterioration in the asset quality, the bank's solvency has weakened with net non-performing advances (NNPAs)/Net worth of 30.4% as on March 31, 2025 vis-à-vis 0.2% as on March 31, 2024. However, Utkarsh continues to maintain an adequate capitalisation profile with the reported capital-to-risk weighted assets ratio (CRAR) at 20.9% as of March 2025. Further, it is in the process of raising Tier I equity capital up to Rs. 750 crore in the near-term, which shall help it maintain a prudent capitalisation profile while providing for the deterioration in the asset quality.

ICRA also takes note of the gradual improvement in Utkarsh's deposit franchise with the share of retail deposits {retail term deposits + current account savings account (CASA)} increasing to ~71% as of March 2025 from ~66% as of March 2024. The share of CASA in total deposits stood at ~22% as on March 31, 2025, similar to the March 2024 level. Going forward, the bank's ability to improve the share of the relatively lower-cost CASA deposits and keep the deposit profile granular shall remain important.

Key rating drivers and their description

Credit strengths

Adequate capitalisation – The bank continues to maintain an adequate capitalisation profile with a capital adequacy ratio of 20.9% (Tier I of 17.9%) as on March 31, 2025 (22.6% (Tier I: 20.9%) as on March 31, 2024) vis-à-vis the regulatory requirement of 15% (Tier I: 7.5%). Its gearing (including deposits) has, however, been increasing and stood at 8.0 times as on March 31,

2025 vis-à-vis 6.5 times as on March 31, 2024, in light of the muted profitability in FY2025. ICRA notes that the bank is in the process of raising Tier I equity capital up to Rs. 750 crore in the near term, which shall help it maintain a prudent capitalisation profile while providing for the deterioration in the asset quality. ICRA expects Utkarsh to remain adequately capitalised while maintaining sufficient buffer over the regulatory requirements as it continues to scale up its operations.

Increasing share of non-microfinance portfolio – The bank continues to scale up its portfolio while diversifying its product offerings and reported assets under management of Rs. 19,666 crore as on March 31, 2025 (Rs. 18,299 crore as on March 31, 2024). Over the years, Utkarsh has been scaling up its relatively newer products, such as loans to micro, small and medium enterprises (MSMEs), housing loans, construction equipment (CE) and commercial vehicles (CVs), etc. Consequently, the share of the relatively riskier microfinance segment has been declining gradually and stood at 50% of the portfolio as on March 31, 2025 (62% as on March 31, 2024; 66% as on March 31, 2023; 77% as on March 31, 2022); ICRA expects the trend to continue. Nonetheless, Utkarsh's ability to maintain the asset quality in the relatively newer product segments remains monitorable.

Credit challenges

Deterioration in asset quality; geographically concentrated portfolio – Utkarsh's asset quality deteriorated in FY2025 with the gross NPAs (GNPAs) and NNPAAs increasing to 9.4% and 4.8%, respectively, as on March 31, 2025 from 2.5% and 0.03%, respectively, as on March 31, 2024. The solvency ratio (NNPAs/Net worth) rose to 30.4% as on March 31, 2025 from 0.2% as on March 31, 2024. This was primarily on account of higher slippages in the microfinance portfolio due to various factors including, but not limited to, adverse climatic conditions, operational challenges, worsening of credit discipline and overleveraging of borrowers. Further, the bank's microfinance portfolio remains geographically concentrated with the share of Bihar and Uttar Pradesh remaining high at 45% and 28%, respectively, as on March 31, 2025.

ICRA notes that Utkarsh has taken certain corrective measures, including the tightening of customer selection criteria, strengthening of the collections team, etc. ICRA also takes note that the current-bucket collection efficiency (excluding prepayments), which stood at 99.1% in Q4 FY2025, and incremental inflows to the SMA bucket have slowed down. Nonetheless, the near-term performance shall remain monitorable, considering the tightened guardrails for the microfinance sector.

Muted profitability – Utkarsh reported a nominal profit of Rs. 24 crore in FY2025 compared to Rs. 498 crore in FY2024. ICRA takes note of the change in the accounting policy with regard to processing fees and allied expenses and the decline in the provision coverage ratio, which helped the bank report a nominal profit in FY2025. The earnings profile was significantly impacted by the deterioration in the asset quality. Credit costs increased to 3.8% in FY2025 from 1.6% in FY2024 on account of higher provisioning and write-offs, leading to muted profitability. Further, with the increase in the relatively lower-yielding non-microfinance portfolio, the overall yields have been declining. This, along with the rise in the cost of average interest-bearing funds, led to a decline in Utkarsh's lending spread and net interest margin. With a sizeable part of the portfolio in the overdue category, ICRA expects the bank's credit costs to remain elevated and earnings profile to remain under pressure in the near term.

Ability to improve CASA share in deposits – Utkarsh has successfully built a large deposit base, constituting 92% of its total borrowings as on March 31, 2025, up from 90% as on March 31, 2024. The overall deposit base increased to Rs. 21,566 crore from Rs. 17,473 crore during the above-mentioned period. However, the share of CASA remained relatively low at 22% as on March 31, 2025 (21% as on March 31, 2024). ICRA takes note of the improving granularity of deposits with CASA + retail term deposits increasing to 71% as on March 31, 2025 from 66% as on March 31, 2024. The share of the top 20 depositors has also been gradually reducing and stood at 16% as on March 31, 2025 (18% as on March 31, 2024; 21% as on March 31, 2023). Nevertheless, improving the granularity of the deposits further while sustainably increasing the share of CASA will be important from a credit perspective.

Liquidity position: Strong

The liquidity coverage ratio was healthy at 168.7% on a daily average basis for the quarter ended March 31, 2025. The net stable funding ratio (NSFR) stood at 120.8% as on March 31, 2025, remaining above the regulatory level of 100%. The bank's structural liquidity statement, as on March 31, 2025, did not show any negative cumulative mismatches for a period of up to one year. Utkarsh's liquidity profile is supported by the large portion of relatively shorter-tenor assets. It reported a credit-to-deposit (CD) ratio of 91%, as on March 31, 2025, against 94% in March 2024. The liquidity profile is also supported by the availability of funding lines from financial institutions (FIs).

Environmental and social risks

Environmental considerations – Given Utkarsh's service-oriented nature of business, its direct exposure to environmental risks as well as those stemming from regulations or policy changes is not material. While the bank is not materially exposed to physical climate risks, it indirectly encounters environmental risks through its portfolio of assets. Further, its lending typically involves short-to-medium-term durations, enabling it to adjust and incrementally invest in less environmentally vulnerable businesses.

Social considerations – Data security and customer privacy are among the key sources of vulnerability for banks, including Utkarsh, 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 banks to reduce their operating costs. However, subpar execution of information technology strategies and the inability to meet customer requirements adequately may result in more costs than benefits. On the positive side, Utkarsh 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 underserved segments could create growth opportunities. However, these opportunities must be seen in conjuncture with asset quality risks that could impact the bank's credit quality.

Rating sensitivities

Positive factors – ICRA could revise the outlook to Stable if the bank demonstrates a sustained improvement in its asset quality and profitability indicators.

Negative factors – Further deterioration in the asset quality or sustained weakening in the profitability (return on assets (RoA) below 1%) could negatively impact the ratings. A significant deterioration in the capitalisation profile could also exert pressure on the ratings.

Analytical approach

Analytical approach	Comments
Applicable rating methodologies	ICRA's credit rating methodology for banks and financial institutions
Parent/Group support	Not applicable
Consolidation/Standalone	Standalone

About the company

Incorporated in 2009, Utkarsh Micro Finance Limited received a small finance bank (SFB) licence from the Reserve Bank of India (RBI) in November 2016 and completed the conversion to an SFB in January 2017. The bank is headed by Mr. Govind Singh, who was earlier the business head of micro-banking at ICICI Bank Limited. Operating in 27 states/Union Territories (UTs), as on March 31, 2025, Utkarsh offers deposits, micro-banking loans, micro, small and medium enterprise (MSME) loans, affordable housing loans and corporate loans, among other products. It had a portfolio of Rs. 19,666 crore as on March 31, 2025, with micro-banking loans (including micro-banking loans sourced by business correspondents) comprising 50% (62% as

on March 31, 2024) of the same. As for liabilities, the bank had a deposit base of Rs. 21,566 crore as on March 31, 2025 (Rs. 17,473 crore as on March 31, 2024), with term deposits accounting for 78% (80% as on March 31, 2024).

Key financial indicators (audited)

Utkarsh Small Finance Bank Limited	FY2023	FY2024	FY2025
Total income	2,804	3,579	4,365
PAT	405	498	24
Total assets	19,118	23,903	28,127
CET I	18.3%	21.0%	17.9%
CRAR	20.6%	22.6%	20.9%
PAT/ATA	2.4%	2.3%	0.1%
Gross NPAs	3.2%	2.5%	9.4%
Net NPAs	0.4%	0.03%	4.8%

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

Note: Total assets excludes revaluation reserves

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2026)				Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Date & rating in FY2026		Date & rating in FY2025		Date & rating in FY2024	Date & rating in FY2023
				May 22, 2025	Apr 2, 2025	Jun 6, 2024	Apr 1, 2024	Apr 13, 2023	Jun 28, 2022
1	Subordinated debt programme	Long term	400.00	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Positive)
2	Certificates of deposit programme	Short term	1,000.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity indicator
Subordinated debt programme	Simple
Certificates of deposit 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
INE735W08038	Subordinated debt	Jun-26-2020	12.50%	Jun-26-2027	195.00	[ICRA]A+ (Negative)
Yet to be issued	Subordinated debt	NA	NA	NA	5.00	[ICRA]A+ (Negative)
INE735W08053	Subordinated debt	Jun-28-2024	11.00%	Jun-28-2031	200.00	[ICRA]A+ (Negative)
INE735W16635	Certificates of deposit	Oct-29-2024	8.50%	Oct-29-2025	50.00	[ICRA]A1+
INE735W16635	Certificates of deposit	Nov-05-2024	8.50%	Oct-29-2025	25.00	[ICRA]A1+
INE735W16635	Certificates of deposit	Nov-06-2024	8.50%	Oct-29-2025	25.00	[ICRA]A1+
INE735W16643	Certificates of deposit	Nov-11-2024	8.50%	Nov-11-2025	50.00	[ICRA]A1+
INE735W16650	Certificates of deposit	Dec-30-2024	8.00%	Sep-18-2025	30.00	[ICRA]A1+
INE735W16643	Certificates of deposit	Mar-05-2025	8.15%	Nov-11-2025	35.00	[ICRA]A1+
INE735W16668	Certificates of deposit	Mar-21-2025	8.05%	Jun-20-2025	50.00	[ICRA]A1+
INE735W16676	Certificates of deposit	Mar-26-2025	8.32%	Dec-08-2025	35.00	[ICRA]A1+
Yet to be issued	Certificates of deposit	NA	NA	7-365 days	700.00	[ICRA]A1+

Source: Utkarsh

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

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