



State Bank of Hyderabad

Instrument	Amount (Rs. crore)	Rating Action
BASEL III Compliant Tier II Bonds Programme	393	[ICRA]AAA (hyb) (stable); assigned

ICRA has assigned the [ICRA]AAA (hyb) (pronounced ICRA triple A hybrid) rating with Stable outlook to the Rs.393 crore Tier II Bonds Programme of State Bank of Hyderabad (SBH/"the bank"). The letters "hyb" in parenthesis suffixed to a rating symbol stand for "hybrid", indicating that the rated instrument is a hybrid subordinated instrument with equity-like loss-absorption features; such features may translate into higher levels of rating transition and loss-severity vis-à-vis conventional debt instruments. The rated Tier 2 bonds are expected to absorb losses once "Point of Non Viability" (PONV) trigger is invoked. ICRA also has [ICRA]AAA (pronounced ICRA triple A) rating with stable outlook outstanding for the Rs. 1400 crore Lower Tier II bonds, MAAA (pronounced ICRA triple A) rating to the term deposit programme and [ICRA]A1+ (pronounced ICRA A one plus) rating to the Rs. 15,000 crore Certificate of deposit (CD) programme of SBH.

The highest credit quality ratings of SBH continue to draw strength from its SBI parentage* and the advantages it enjoys on account of operational and management synergies with its parent. The ratings factor in the banks established franchise in Andhra Pradesh, which enables access to low cost CASA deposits (31% in Dec-14) and access to fee-based income from Government of Telangana (GoT) transactions. SBH's strong franchise, backed by the 'SBI' brand is likely to ensure adequate growth in the credit and deposits of the bank. ICRA has noted with concern deterioration in SBH asset quality profile over the past couple of years (Gross NPA% plus 35% of standard restructured advances increased to 7.2% as on December 2014 against 4.6% in March 2013). It would be critical for SBH to improve its asset quality profile. As for capitalization, SBH's capitalisation profile remains adequate (Tier I capital at 8.73% and CRAR at 10.85%†) against the current regulatory minimum requirement as per Basel III norms as of December 2014. However SBH would be dependent on SBI for fresh capital raising for meeting higher capital requirements under Basel III norms as well as for business growth. Nevertheless, SBH's relatively better internal capital generation (SBH's return on net worth was 12.6% during 9M FY15) lowers its external CET requirement during FY15-FY19 to around 30-40% of its net worth as on March 2014.

SBH reported a credit growth of 6% in FY2014 and 2% in 9M FY2015 to Rs.97,259 crore as the bank adopted a cautious lending approach in a challenging operating environment. As on December 31, 2014 SBH's gross NPA% was 5.4% (against the PSBs average of 5.1%), and declined from 5.9% in March 2014 largely on account of sale of NPAs by the bank to Asset Reconstruction Companies (ARCs) in 9M-FY15. ICRA notes a moderation in the NPA generation rate of the bank in 9M-FY15 to 3.4% (against 5.5% in FY14), although these remain relatively high. The weakness in the bank's asset quality largely stems from its exposures in the corporate and SME segments, where gross NPA% as on December 2014 was 7.63% and 7.98% respectively. In the agriculture and retail segment gross NPA% was 2.38% and 0.99% in December 2014 respectively. ICRA notes that credit culture of agriculture borrowers in the states of Andhra Pradesh and Telangana could turn adverse given the announcement of debt waivers of agriculture loans by the respective state governments, which could impact recovery rates in the segment. SBH's standard restructured advances stood at about 5.6% in December 2014 are lower than the public sector bank average of 6.5% in December 2014. Going forward would be important for SBH to control its NPA generation rate and recover from standard restructured advances. SBH's net NPA declined to 2.43% in December 2014 from 3.12% in March 2014 as a result its solvency ratio (net NPA to net worth) improved to a moderate 25.6% in December 2014 from 35.7% in March 2014. SBH has healthy deposits profile with good proportion of low cost deposits or CASA‡ (328% of total deposits as of December 2014) and although dependence on whole sale deposits (bulk deposits plus certificate of deposits) is fairly high at 28.8% of SBH's total deposits as on December 2014.

* SBI has 100% equity stake in SBH

† Including 9M, FY15 profits, Tier I and CRAR increases to 9.64% and 11.76% respectively

‡ Current Account and Savings Account



SBH has reported adequate profitability profile vs. peers (PAT/ATA[§] of 0.81% during 9MFY15 against 0.73% in during FY14) on the back of adequate NIMs (2.96% in 9M-FY15) and low operating expenses (1.82% in 9M-FY-15). SBHs NIMs are supported by healthy share of CASA deposits and consequent low cost of funds. In ICRA's view, over the medium-term earnings of the bank would be contingent upon its ability to maintain NIMs as well as asset quality profile. SBH's liquidity profile is comfortable supported by healthy deposits profile. ICRA expects the bank to maintain an adequate liquidity profile on the back of its strong parentage and the franchise imparting a stable deposit base.

Bank Profile

State Bank of Hyderabad was constituted as Hyderabad State Bank on August 1941 under Hyderabad State Bank Act, 1941. The first branch of the Bank was opened at Gunfoundry, Hyderabad on 5th April, 1942. In 1953, the Bank took over the assets and liabilities of the Hyderabad Mercantile Bank Ltd. In the same year, the Bank started conducting Government and Treasury business as agent of Reserve Bank of India. In 1956, the Bank was taken over by Reserve Bank of India as its first subsidiary and its name was changed from Hyderabad State Bank to State Bank of Hyderabad. The Bank became a subsidiary of the State Bank of India (SBI) on the 1st October 1959 and is the largest subsidiary in terms of balance sheet size as on December 31, 2014. SBH, a 100% subsidiary of SBI, has a strong branch penetration in Telangana and Andhra Pradesh. During the financial year ended March 31, 2014 SBH reported a reported net profit of Rs 1102 crore on an asset base of Rs. 1,41,489 crore compared to a profit of Rs. 1,250 crore on an asset base of Rs. 1,36,078 crore in the previous financial year. During the nine month period ended December 31, 2014 the bank reported a profit of Rs. 872 crore against a profit of Rs. 576 crore during the corresponding period in the previous financial year.

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[§] Profit after Tax / Average Total Assets

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