

Oriental Bank of Commerce

Instrument	Amount	Rating Action
Basel III Compliant Tier 1 Bonds Programme	Rs 1,000 crore	[ICRA]A+(hyb) (Negative) Assigned
Basel III Compliant Tier 2 Bonds Programme	Rs 3,000 crore	[ICRA]AA(hyb) (Negative)
Basel III Compliant Tier 1 Bonds Programme	Rs 1,000 crore	[ICRA]A+(hyb) (Negative)
Basel II Lower Tier 2 Bonds Programme	Rs 1,700 crore	[ICRA]AA (Negative)
Basel II Upper Tier 2 Bonds Programme	Rs 1,000 crore	[ICRA]AA- (Negative)
Basel II Perpetual Bonds Programme	Rs 250 crore	[ICRA]AA- (Negative)

ICRA has assigned rating of [ICRA]A+(hyb) (pronounced ICRA A plus hybrid) with a negative outlook to the Rs. 1,000 crore Basel III Compliant Additional Tier 1 Bonds Programme of Oriental Bank of Commerce (OBC)†.

ICRA has reaffirmed the [ICRA]AA(hyb) rating for the Rs 3,000 crore Basel III compliant Tier 2 bonds programme, [ICRA]AA (pronounced ICRA double A) for Rs 1,700 crore Basel 2 Lower Tier 2 Bonds programme, [ICRA]AA- (pronounced ICRA double A minus) for Rs 1,000 crore Basel 2 Upper Tier 2 bonds programme and Rs 250 crore Basel 2 Perpetual bonds programme, and [ICRA]A+(hyb) (pronounced ICRA A plus hybrid) to the Rs 1,000 crore Basel 3 Additional Tier 1 (AT1) bonds programme of OBC. The outlook on aforementioned ratings has been revised from 'Stable' to 'Negative'.

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.

Furthermore, the rating for the Basel III compliant Tier I bonds is two notches lower than the Basel III compliant Tier II bonds of the bank as these instruments have the following loss absorption features that make them riskier.

- Bank has full discretion at all times to cancel distribution/payments and cancellation of discretionary payments shall not be an event of default.
- The minimum capital conservation ratio applicable to the banks may restrict the bank from servicing these Tier I bonds in case the Common Equity Tier-I falls below limit as prescribed by RBI.

These Tier I bonds are expected to absorb losses through Write-Down Mechanism at the Objective Pre-Specified Trigger Point fixed at Bank's Common Equity Tier-I ratio as prescribed by RBI, 5.5% till March 2019 and thereafter 6.125% of Total Risk Weighted Assets of the Bank or when the "Point of Non Viability" (PONV) trigger is breached in the RBI's opinion.

The revision in outlook is on account of the weakness in OBC's asset quality profile, further significant weakness in same could lead to a rating change.

The ratings factor in majority ownership by Government of India (GoI) which provides a strong likelihood of sovereign support to the bank and its established franchise in Northern India imparting it a stable deposits profile and comfortable liquidity position.

OBC's current capitalization profile (Tier 1 capital at 9.16% as on June 30, 2016) is comfortable as against regulatory minimum requirement as of now; however the bank would need to raise sizeable Tier 1 capital over FY17-FY19 to meet Basel 3 norms as well as for growth. In ICRA's estimate OBC will need to raise Tier 1 capital of Rs 5,000-6,000 crore over FY17-FY19, the requirement is very high (120-140% in relation to current market capitalization of the bank). OBC's ability to raise capital from government as well as non-government

† "For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications"

sources will have strong bearing on its ability to grow at reasonable pace as the Govt ownership at 58.38% provide limited headroom to raise capital from non-government sources.

The ratings are constrained on account of significant weakness in asset quality profile and consequent impact on profitability during last two years. OBC's stressed advances (Gross NPA % + Standard restructured advances¹) are high at around 17.4% as on June 30, 2016 (increased further from 16.3% as on March 2016) vs. PSBs average of around 14% as on same date.

OBC's asset quality profile weakened further in Q1, FY17 as fresh NPA generation remained high, around 60% of fresh NPA generation in Q1, FY17 was from non-restructured advances. OBC's Gross NPA % and Net NPA % increased from 9.57% and 6.70% respectively as on March 31, 2016 to 11.45% and 8.11% as on June 30, 2016. In addition, OBC's standard restructured advances² at 5.9% are higher than peers (PSBs average of ~4%) which along with other vulnerable exposure could lead to relatively high fresh NPA generation over next 1-2 years. At the same time, OBC's strong focus on recoveries from NPAs / standard restructured; some improvement in operating environment for some of the credit intensive sectors, implementation of Bankruptcy code and RBI's recent regulation for Scheme of Sustainable Structuring of Stressed assets (S4A) could ease some pressure on asset quality profile over medium term.

OBC's provision cover at 49%³ (31.8% excluding written off accounts vs. PSBs average of 40.6%) is low at June 30, 2016, expected build up of provision cover in FY17 could lead to continued pressure on profitability profile in FY17. OBC's credit cost was very high at 1.45% of ATA in FY16. OBC's annualized operating profits in relation to net NPAs have dropped to 26% in Q1, FY17 (vs. 30% in Q4, FY16 and 35% in Q3, FY16). While OBC was one of the PSBs which reported net profits in FY16⁴, OBC's profitability was very low at PAT/ATA of 0.07% and return on net worth of 1.2% in FY16 and 0.17% and 3.0% in Q1, FY17. OBC's profitability likely to remain weak over next 1-2 years as credit cost expected to remain at elevated levels.

OBC has been able to maintain stable NIMs⁵ in FY16 (at around ~2.3%) vs. FY15 on the back of improvement in deposits profile through reduction in large ticket deposits and some improvement in share of CASA⁶ deposits. Share of CASA deposits for OBC, though increased from 24.2% as on March 2015 to 25.2% as on March 31, 2016 and 25.9% as on June 30, 2016, still remain lower vs. PSBs average of more than 30% as on March 2016. OBC's core operating profitability was around 1.4% of ATA in FY16 vs. 1.6% of ATA in FY15.

Bank Profile

Oriental Bank of Commerce was incorporated in 1943 and nationalised in April 1980. Government of India held 58.38% stake in OBC as on June 30, 2016. In August 2004, financially depressed Global Trust Bank was merged with OBC and prior to that Punjab Co-operative Bank and Bari Doab were merged with OBC in 1997. OBC has a strong franchise in northern India, which allows it to have a stable deposit base and gives it access to a wide range of customers. The bank's presence in the South and West has improved following its August 2004 acquisition of GTB. As on June 30, 2016, OBC has a network of 2,351 branches and 2,585 ATMs; more than half of its branches are in rural and semi urban areas.

OBC reported a profit after tax (PAT) of Rs 156.08 crore in FY16 on a total asset base of Rs 2,36,034 crore as on March 31, 2016 as against PAT of Rs 497.08 crore in FY15 on a total asset base of Rs. 2,29,892 crore as on March 31, 2015. During Q1, FY17 OBC reported PAT of Rs 100.69 crore vs. PAT of Rs 257.84 crore during Q1, FY16. OBC's Gross and Net NPA % were 11.45% and 8.11% as on June 30, 2016. OBC's Tier 1 capital % and CRAR % were 9.16% and 12.40% as on June 30, 2016.

August 2016

¹ Excluding SEBs

² Excluding SEBs

³ Including technical write-offs

⁴ Out of 26 PSBs, 12 reported net profit while other 14 reported net losses in FY16

⁵ Net Interest Income / Average Total Assets

⁶ Current Account Saving Account



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