Kotak Mahindra Bank Limited

Instrument	Amount Rated (In Rs Crore)	Amount Outstanding* (In Rs Crore)	Rating Action September 2016
Infrastructure Bonds	1500	962	[ICRA]AAA with stable outlook reaffirmed
Lower Tier II Bonds	625	403	[ICRA]AAA with stable outlook reaffirmed
Upper Tier II Bonds	150	136	[ICRA]AA+ with stable outlook reaffirmed

As on August 31, 2016

ICRA has reaffirmed the rating of [ICRA]AAA (pronounced as ICRA triple A) with a stable outlook for the Rs 1,500 crore infrastructure bonds and Rs 625 crore of lower tier II bonds of Kotak Mahindra Bank Limited (KMBL). ICRA has also reaffirmed the rating of [ICRA]AA+ (pronounced as ICRA double A plus) with stable outlook for the Rs 150 crore upper tier II bonds programme of KMBL. The one notch lower rating assigned to the upper tier II bonds reflects the specific features of the instrument, wherein debt servicing is additionally linked to meeting the regulatory norms on capitalization and reported profitability.

The ratings take into account the combined financials and operational performance of the Kotak Mahindra group of companies. The ratings also reflect KMBL's strong capitalization level both in terms of absolute net worth as well as tier I capital, its comfortable profitability, proven ability to manage asset quality through cycles, improving granularity in the deposits profile and the diversified revenue profile of the group. The credit strengths are partially offset by the bank's relatively high – although decreasing – dependence on wholesale funding.

Following the merger of ING Vysya Bank Limited (IVBL), the bank's merged credit portfolio registered a growth of ~11 in FY2016 and sequential ~2% QoQ in Q1FY2017. The growth was low on account of consolidation of some accounts and focus on the stress portfolio of the erstwhile IVBL. As on June 30, 2016, the overall retail advances of the bank stood at 41% (44% standalone as on March 31, 2015) with balance being corporate. Post merger, the share of Business banking (SME) advances as on June 30, 2016 increased to 14% (10% as on March 31, 2015). The management expects the bank's loan book to grow at ~20% during FY2017 with growth across segments.

The bank's asset quality indicators weakened with gross NPA% of 2.50% and net NPA% of 1.2% as on June 30, 2016 when compared to standalone levels of 1.85% and 0.92% respectively as on March 31, 2015. The dip in asset quality has been largely on account of the merger with IVBL. The bank has proactively recognised a large part of IVBL's stressed accounts leading to high slippages in FY2016. KMBL's provision cover stood at 52% as on June 30, 2016 (51% as on March 31, 2015). The bank had a small standard restructured book of Rs 160 crore (~0.13% of overall advances) as on June 30, 2016. ICRA takes comfort from the bank's corporate exposures being largely in the form of working capital and corporate group level advances and the absence of any significant exposure to project companies. Any significant deterioration in asset quality indicators will remain a key rating sensitivity.

Post the deregulation of savings rates, the share of retail deposits in the bank's deposit base increased to 37.4% as on June 30, 2016 (~36% as on March 31, 2015). Including ~6.2% of sweep deposits, the overall low cost deposits of the bank stood at ~43.6% as on June 30, 2016. Consequently, the share of CASA and term deposits with ticket sizes lower than Rs. 5 crore increased to 70% of overall deposit base in June 2016 (70% in March 2016 and March 2015), indicating improving granularity in the overall resource profile. However, the bank's cost of deposits continues to remain higher than its peers on account of the higher savings account rate offered by it. Post merger, the bank's branch network increased from 684 in March 2015 to 1333 in June 2016. By March 2017, the bank intends to further increase the number of branches to ~1400 and its CASA to over 40% supported by the increase in CASA traction in eIVBL branches and continued branch expansion.

The capitalisation of the bank is strong with a capital adequacy ratio (CRAR) of 16.8% and common equity tier I (CET I) of 15.8% under Basel III as on June 30, 2016. On a consolidated basis, including unaudited profits, the CRAR stood at 17.3% with CET I of 16.5%. In ICRA's view, KMBL's current capital adequacy ratio with a high proportion of Tier-I capital provides it adequate room to scale up its lending operations while maintaining regulatory capital requirement in addition to supporting the net interest margins (NIMs).

While the earnings profile for the bank remained comfortable, it reported PAT of ~1.6% of ATA in the TTM Jun-16 as compared to ~1.9% in FY2015; the decline in profitability was on account of lower net interest margins following the merger and one off credit costs and merger related expenses. Going ahead, KMBL's profitability is likely to improve in the medium term with synergies of the merger flowing in.

About Kotak Mahindra Bank Limited
KMBL is the flagship company of the Kotak group. KMBL began operations in 1986 as a bill discounting and leasing NBFC, Kotak Mahindra Finance Limited which was converted into a bank in 2003. Effective April 1, 2015, ING Vysya Bank was merged with KMBL.

KMBL has a network of over 1,333 branches in June 2016. The bank's advances stood at Rs. 120,765 crore with corporate advances accounting for 59% of the total. KMBL reported a PAT of Rs. 2,090 crore for FY2016 as against PAT of Rs. 1,866 crore for FY2015. For Q1FY2017, KMBL reported a PAT of Rs. 742 crore. KMBL's net worth stood at Rs. 24,744 crore as on June 30, 2016.

About Kotak Group
Kotak group is one of India's leading full services financial conglomerate, with significant presence in securities and investment banking space while it is currently growing its banking, asset management and insurance businesses. The group derives synergies from its various platforms, given their presence across the financial spectrum. Other than KMBL, the key subsidiaries of Kotak group include Kotak Mahindra Prime Limited (car financing), Kotak Securities Limited (retail and institutional broking and portfolio management services), Kotak Mahindra Investments Ltd. (commercial real estate lending and securities based lending), Kotak Mahindra Capital Company (investment banking), Kotak Mahindra Old Mutual Life Insurance Ltd (life insurance) , Kotak Mahindra General Insurance Company Ltd (general insurance), Kotak Mahindra Asset Management Company (asset management business) and Kotak Private Equity Group (private equity business).

At the consolidated group level, KMBL's advances constitute 82% of overall advances of Rs 1,47,004 crore of the group as on June 30, 2016. On a consolidated group basis, Kotak group reported a PAT of Rs 3,459 crore in FY2016 as compared to Rs 3,045 crore in FY2015. For Q1FY2017, the group reported a PAT of Rs 1,067 crore. The group's consolidated net worth stood at Rs 34,443 crore as on March 31, 2016.

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