ICRA

October 05, 2017

RBL Bank Limited Revised

Summary of rated instruments

Instrument*	Rated Amount (Rs. crore)	Rating Action
Certificate of Deposit Programme	4,000 (enhanced from 3,000)	[ICRA]A1+; assigned
Basel III Compliant Tier II Bond Programme	800	[ICRA]AA- (hyb) (stable); upgraded from [ICRA]A+ (hyb) (positive)
Medium Term Fixed Deposit Programme	-	MAA (stable); upgraded from MAA- (positive)
Short Term Fixed Deposit Programme	-	[ICRA]A1+; reaffirmed
Total	**4,800**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has upgraded the rating for the Rs. 800 crore Basel III Compliant Tier II bond programme of RBL Bank Limited (RBL) to [ICRA]AA- (hyb) from [ICRA]A+ (hyb). ICRA has also upgraded the rating of the bank's medium term fixed deposit programme to MAA from MAA-. ICRA has also assigned the rating of [ICRA]A1+ for the enhanced certificate of deposit programme of Rs. 4,000 crore (enhanced from Rs. 3,000 crore) of RBL. ICRA has also reaffirmed the rating of [ICRA]A1+ for the short term fixed deposit programme of RBL. The outlook on the long-term and medium-term ratings has been changed to Stable from Positive earlier.

Rationale

The upgrade follows the equity capital raising of Rs. 1,680 crore by the bank through a preferential issue in August 2017, which has resulted in an improvement in the current capitalisation profile and would also support future growth. The positive outlook on the long term and medium term ratings earlier, had factored in the gradual improvement in the bank's liability profile supported by lower deposit concentration, reducing share of bulk deposits and elongation in the average maturity of deposits. Notwithstanding the gradual improvement in its liability profile, the deposits of the bank remain concentrated with relatively high share of bulk deposits and lower proportion of low-cost deposits in its resource profile. The bank's asset quality indicators also remain comfortable despite some weakening in the microfinance loan book during Q1FY2018.

The ratings continue to be supported by the bank's long track record, its experienced senior management team, diversified non-interest revenue sources and strong capitalisation levels following the equity raising. ICRA takes note of the concentration of advances in terms of geography and corporate groups. While the geographical concentration continues to reduce with Maharashtra, Karnataka and Delhi/NCR accounting for 58.20% of the advances as on June 30, 2017 as against 96.4% as on March 31, 2013, the bank's top-20 group exposures remain high at 29% of the total exposures as on June 30, 2017. ICRA nevertheless notes that the top-20 group exposures are towards corporates with good credit quality. Given the robust growth in the last four years, the bank's loan book is relatively unseasoned with a high share of unsecured portfolio (~32% of advances as on June 30, 2017); a majority of the unsecured book is in the form of microfinance loans where the borrower profile is vulnerable to economic shocks. ICRA takes notes of the weakening in asset quality in the microfinance loans post demonetisation and the expected higher credit costs of 2-2.50% on this portfolio, which will translate to a credit cost of 0.11% for the bank in the current fiscal.

Given the bank's high growth plans, its ability to diversify the mix of assets and liabilities, while maintaining comfortable asset quality and capitalisation will remain the key rating positives. Conversely, a sharp deterioration in asset quality as the loan book seasons leading to a decline in profitability or an increase in concentration of exposures or liabilities will be rating negatives.

Key rating drivers

Credit strengths

- **Steadily improving scale of operations -** The bank's loan book grew by 39% in FY2017 to Rs. 29,449 crore as on March 31, 2017. The advances grew further by 40% on a YoY basis during Q1FY2018, to Rs. 31,108 crore as on June 30, 2017. Within the loan book, the share of wholesale advances stood at 60% as on June 30, 2017. Although the credit off take in the wholesale segment remained muted for the industry, the bank reported a growth owing to its lower base and by catering to the short term requirements of corporate customers. With the bank's focus being on working capital loans, 84% of the overall advances were of less than 3 year tenure as on June 30, 2017. Of the total portfolio, 68% of the portfolio was secured as on June 30, 2017. The unsecured portfolio includes loans to MFIs, BILs, credit card as well as bank lines for certain highly rated large corporate borrowers.
- **Strong capitalisation supported by the capital raising in August 2017 -** The bank's capital ratios (Tier 1 and CRAR as % of risk weighted assets) stood at 11.10% and 13.40% respectively as on June 30, 2017, which were higher than the regulatory levels. The solvency remained strong with net NPAs/net worth of 5.6% as on June 30, 2017 (4.8% as on June 30, 2016 and 4.4% as on March 31, 2017), and was better than industry average. However, given the capital required to fund the targeted growth, the bank raised Rs. 1,680 crore in August 2017, by way of a preferential issue to reputed institutional investors. With the capital infusion, the bank is now adequately capitalised to meet its medium term growth targets. Post the capital rising, the bank's Tier 1 and CRAR are expected to have increased by ~4% of risk weighted assets.
- **Steady improvement in profitability driven by lower cost of funds -** The company's yield on advances declined to 10.2% during Q1FY2018 (10.7% in Q1FY2017) given the declining interest rate environment. However, with a higher decline in cost of funds to 6.3% during Q1FY2018 (7.2% in Q1FY2017), the bank's net interest margins[1] (NIMs) improved to 3.1% during Q1FY2018 (2.5% in Q1FY2017). ICRA notes that the surplus liquidity and the higher share of bulk deposits has contributed to the higher decline in the bank's cost of funds. With the improvement in NIMs and the significant growth in advances, the bank's net interest income (NII) registered a YoY growth of 55% during Q1FY2018 (49% in FY2017). Strong NII growth and a high treasury income of Rs. 75 crore during the quarter (Rs. 48 crore during Q1FY2017) resulted in an improvement in profit after tax / ATA (PAT/ATA) to 1.16% during Q1FY2018 (1.00% in Q1FY2017).

[1] as % of average total assets – ATA

- **Comfortable asset quality -** The bank's asset quality weakened slightly with gross NPAs increasing to 1.46% as on June 30, 2017 (1.20% as on March 31, 2017) with slippages increasing in the Development Banking and Financial Inclusion (DB&FI) segment during the quarter. With the higher slippages, the net NPAs increased to 0.80% as on June 30, 2017 (0.64% as on March 31, 2017). The bank's standard restructured assets stood at 0.24% of the total advances as on June 30, 2017 (0.25% as on March 31, 2017). The bank has not done any SDR, S4A or 5/25 refinancing during Q1FY2018. The Bank has done only one SDR in Q3FY2017. RBL's security receipts stood at 0.02% as on June 30, 2017. The bank also does not have any exposure to the 12 accounts identified by the Reserve Bank of India for insolvency proceedings. Overall, despite the weakening, the bank's asset quality remains comfortable.

Credit weaknesses

- **Concentration of advances, albeit gradually reducing -** The bank's operations were initially concentrated in the Maharashtra and North Karnataka region. In the past 5 years, it has opened branches in the commercial zones of the country like Delhi, Chennai and other metros; exposures in these branches have started increasing, resulting in lower geographic concentration. Currently, Maharashtra and Delhi account for a majority of the bank's advances, at around 50% as on June 30, 2017 (52% as on March 31, 2016). As on June 30, 2017, the western region contributed 39% of net advances (40% in March 31, 2016) followed by 25% by the North (28%), 20% by South (22%) and 17% by East (10%). RBL's top 20-group exposures accounted for 29% of the total exposure over the past few quarters. Although the concentration of group exposures is relatively high, these are towards higher rated corporates which provides some comfort.
- **Albeit an improvement, resource profile remains concentrated –** Even though the bank's Current Account and Saving Account (CASA) ratio improved to 22% as on June 30, 2017 from 19% as on March 31, 2016, the ratio remains lower than that of many other private sector banks. The rise in RBL's saving deposits was on account of the higher rates on deposits offered, the greater visibility of the bank through increasing branch presence and branding efforts, and partly on account of demonetisation. The share of deposits over Rs. 1 crore remained high (although declining) at 66% as on June 30, 2017 (as compared to 72% as on March 31, 2016).
- **Higher credit costs on the microfinance loan book -** Following demonetisation, the bank's asset quality in the DB&FI segment suffered the most given the unsecured nature of lending and the marginal profile of the borrowers. As on June 30, 2017, the bank had an exposure of Rs. 4,200 crore to the DB & FI segment of which the microfinance portfolio (joint liability group lending) stood at Rs 2,258 crore (53%) while the balance Rs. 1,942 crore was to NBFCs catering to these borrowers. RBL's 30+ dpd for the microfinance portfolio stood at 6.43% (Rs. 145 crore) as on June 30, 2017 and is expected to increase to around 8.5 to 9% by March 2018. Since the bank's direct microfinance lending is sourced through business correspondents (BCs), RBL has first loss default guarantees (FLDG) of 3-5% on its microfinance book furnished by the BCs. The bank expects potential losses in FY2018 of around 2% to 2.5% of the outstanding micro-banking portfolio after adjusting the FLDGs. A loss of 2.5% on the micro-banking book amounts to ~Rs. 56 crore, which at ~1.3% of Tier 1 capital will be low.

- **Operating expenses remain high –** Though the bank's operating cost to income ratio[2] reduced to 57.79% in Q1FY2018 from 62.45% in Q1FY2017, it remains higher than the private sector banks' average of 46.67% in Q1FY2018. While the ratio improved in Q1FY2018, it remains vulnerable to any increase in the cost of bulk deposits in the future. The bank's operating expenses are expected to remain high with significant investments being made in infrastructure, branches and technology in line with the scaling up of operations.

Analytical approach:
For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria
ICRA Rating Methodology for Banks

About the company
RBL Bank Limited is a Kolhapur, Maharashtra based private sector bank established in 1943. Following a management change in 2010, the Bank's corporate office shifted to Mumbai. Since FY2011, it is one of the fastest growing scheduled commercial banks with a presence across 16 Indian states and union territories. As on June 30, 2017, RBL operated through 244 branches and 387 ATMs.

During FY2017, the bank reported a total income of Rs. 4,469 crore and a net profit of Rs. 446 crore (RoE of 13.46%). In Q1FY2018, the bank reported a net profit of Rs. 141 crore as compared with a net profit of Rs. 97 crore in Q1FY2017 with a comfortable regulatory capital adequacy ratio at 13.40% (Tier I capital standing at 11.10%) as on June 30, 2017.

Key Financial Indicators

	FY2016	**FY2017**	**Q1FY2017**	**Q1FY2018**
Net Interest Income	819	1,221	245	378
Profit before tax	428	681	142	217
Profit after tax	292	446	97	141
Net advances	21,229	29,449	22,265	31,108
Total assets	39,161	48,675	38,490	48,952
%CET 1	11.10%	11.40%	10.60%	11.10%
%Tier 1	11.10%	11.40%	10.60%	11.10%
% CRAR	12.94%	13.72%	12.01%	13.40%
% Net Interest Margin / Average total assets	2.47%	2.78%	2.52%	3.10%
%Net Profit / Average total assets	0.88%	1.39%	1.00%	1.16%
%Return on Net Worth	9.78%	13.46%	12.76%	12.78%
% Gross NPAs	0.98%	1.20%	1.13%	1.46%
% Net NPAs	0.59%	0.64%	0.66%	0.80%
% Provision coverage incl technical write offs	40.19%	46.77%	41.50%	45.41%
% Net NPA / Net worth	6.77%	4.38%	4.75%	5.57%

Source: Company data and ICRA research; Amount in Rs. crore
All ratios are as per ICRA calculations

[2] Trading income is excluded from operating income, for computing the operating cost to income ratio

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating history for last three years:
Table:

Sr. No.	Instrument	Current Rating			Chronology of Rating History for the past 3 years						
		Type	Rated amount (Rs. crore)	October 2017	FY2017			FY2016		FY2015	
					March 2017	December 2016	June 2016	February 2016	July 2015	August 2014	July 2014
1	Certificate of Deposits	Short Term	4,000	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Short Term Fixed Deposits	Short Term	NA	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
2	Basel III Compliant Tier II Bond Programme	Long Term	800	[ICRA]AA- (hyb) (stable); upgraded from [ICRA]A+ (hyb) (positive)	[ICRA]A+ (hyb) (positive); outlook revised to positive	[ICRA]A+ (hyb) (stable)	[ICRA]A+ (hyb) (stable)	[ICRA]A+ (hyb) (stable); Assigned	NA	NA	NA
3	Medium Term Fixed Deposits	Long Term	NA	MAA (stable); upgraded from MAA- (positive)	MAA- (positive); outlook revised to positive	MAA- (stable)	MAA- (stable)	MAA- (stable)	MAA- (stable)	MAA- (stable)	MAA- (stable)

Complexity level of the rated instrument:
ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

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Annexure-1
Instrument Details

ISIN No.	Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Rated Amount (Rs. crore)	Current Rating and Outlook
INE976G08049	Basel III tier II bonds	16-Feb-16	10.25%	16-May-22	200.00	[ICRA]AA-(hyb) (stable)
INE976G08056	Basel III tier II bonds	31-Mar-16	10.25%	30-Jun-22	200.00	[ICRA]AA-(hyb) (stable)
INE976G08064	Basel III tier II bonds	27-Sep-16	10.20%	15-Apr-23	330.00	[ICRA]AA-(hyb) (stable)
NA	Basel III tier II bonds	Yet to be placed	-	-	70.00	[ICRA]AA-(hyb) (stable)
NA	Certificate of Deposits	-	-	7-365 days	4000.00	[ICRA]A1+
NA	Short Term Fixed Deposits	NA	NA	NA	NA	[ICRA]A1+
NA	Medium Term Fixed Deposits	NA	NA	NA	NA	MAA (stable)

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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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