October 23, 2020

Central Bank of India: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Lower Tier II Bonds Programme	500.00	500.00	[ICRA]A+ (Negative); reaffirmed
Upper Tier II Bonds Programme	500.00	-	[ICRA]A- (Negative); reaffirmed and withdrawn
Upper Tier II Bonds Programme	1,000.00	-	[ICRA]A- (Negative); reaffirmed and withdrawn
Basel III Tier II Bonds Programme	2,000.00	2,000.00	[ICRA]A+(hyb) (Negative); reaffirmed
Total	**4,000.00**	**2,500.00**	

**Instrument details are provided in Annexure-1*
^rating has been withdrawn as the bank has redeemed the instrument on the exercise of call option

Rationale

The ratings for Central Bank of India (CBI) continue to factor in its majority sovereign ownership (Government of India (GoI) shareholding of 89.78% as on September 30, 2020). The GoI has a demonstrated track record of capital infusion of Rs. 15,203 crore in the bank during FY2018-FY2020 to meet the regulatory capital requirement. The rating reaffirmation also takes into account the bank's well-established deposit franchise with a strong current account and savings account (CASA) base that also augments its strong liquidity profile.

The ratings factor in CBI's weak asset quality with high fresh slippages of ~6.0% of standard advances in FY2020 (7.4% in FY2019). While the annualised fresh slippage generation rate moderated sharply to 0.10% in Q1 FY2021 on the back of standstill asset classification, the outlook for FY2021 remains weak in the backdrop of the weak economic condition. A high share (35% of its advances (in value terms) as on August 31, 2020) of the bank's loan book was under moratorium, which has resulted in significant uncertainty regarding its asset quality in the near term.

Despite declining over the last few years, the net non-performing assets (NNPAs) remained high at 6.76% of net advances as on June 30, 2020. The credit provisions continued to surpass the operating profits, translating into losses in FY2020, which could continue in the near term, given the legacy stressed assets and uncertainty on the asset quality. Despite the losses, the bank's net NPA/core capital improved to 73.96% as on June 30, 2020 from 102.11% as on March 31, 2019 and the Tier I capital improved to 9.22% from 7.49% during this period, supported by the capital infusion by the GoI.

Going forward, with estimated fresh NPA generation of 3-4% in FY2021, the credit costs could exceed CBI's core operating profits. Therefore, the bank's ability to reduce its NNPA below 6% to exit the prompt corrective action (PCA) framework will depend on its ability to make huge recoveries in legacy stressed assets. In ICRA's view, CBI will remain dependent on capital support to exit the PCA framework and its equity capital requirement will remain elevated at ~Rs. 4,200-4,400 crore against which the board has approved a capital raising of Rs. 5,000 crore.

The Negative outlook on the ratings continues to reflect the bank's weak asset quality and solvency profile, which are expected to remain a drag on the overall profitability, especially in the backdrop of the Covid-19-induced economic slowdown. This will also pose sizeable capital requirements for the bank in case it has to exit the PCA framework.

Key rating drivers and their description

Credit strengths

Sovereign ownership with demonstrated capital support from GoI – The ratings continue to factor in the bank's majority sovereign ownership (89.78% equity shares held by the GoI as on September 30, 2020) and the demonstrated track record of capital infusion of Rs. 15,203 crore during FY2018-FY2020 (Rs. 5,258 crore in FY2018, Rs. 6,592 crore in FY2019 and Rs. 3,353 crore in FY2020) to support the capitalisation position. ICRA notes that the capital infusion was made into CBI to enable it to meet the regulatory capital requirements even though the capital infusion by the GoI into some other public sector banks (PSBs) was much higher to enable them to exit the PCA framework. Though CBI raised Rs. 255 crore through a qualified institutional placement (QIP) of equity shares in September 2020, ICRA believes that its capital requirement is much higher to exit the PCA framework.

ICRA expects CBI to require an additional ~Rs. 4,200-4,400 crore to reduce its NNPA ratio below 6% while maintaining the capital ratios above the regulatory requirement (including the capital conservation buffer (CCB) of 2.5% required as on April 1, 2021[1]). However, without a capital infusion, ICRA expects the bank to meet the CRAR of 9.0% even in a scenario of loss. The GoI has announced its recapitalisation plan of Rs. 20,000 crore for FY2021 for PSBs though the bank-wise capital allocation is awaited.

Well-developed deposit franchise with strong CASA deposit base – CBI has a long-standing presence in the Indian banking system with an extensive network of over 4,649 branches, of which ~63% are in the rural (34%) and semi-urban regions (29%), providing access to low-cost CASA deposits. The bank had a strong CASA base of 46.85%[2] compared to the PSBs' average of 40% as on June 30, 2020. While the overall branch network remained stable, excluding a few branches that were closed to contain costs by rationalising relatively inefficient branches, the CASA deposits grew by 11.62% on a YoY basis to Rs. 1.50 lakh crore as on June 30, 2020 (Rs. 1.35 lakh crore as on June 30, 2019). The cost of interest-bearing funds for CBI has been improving vis-à-vis the PSB average and stood at 4.78% in Q1 FY2021 (4.65% for PSBs) compared to 5.09% in FY2020 (4.93% for PSBs).

Credit challenges

Asset quality remains under pressure – The overall stock of NNPAs remained driven by the high slippages and increase in existing NPAs amounting to Rs. 8,151 crore (6.02% of standard advances) compared to Rs. 10,460 crore

[1] The RBI has pushed back the deadline to maintain an additional 0.625% CCB from September 30, 2020 to April 1, 2021
[2] Calculated as CASA/Total Domestic Deposits

(7.42%) in FY2019. The bank's asset quality indicators remained weak with GNPAs of 18.93% and NNPAs of 7.63% as on March 31, 2020 (19.31% and 7.73%, respectively, as on March 31, 2019).

The standstill on asset classification upon the moratorium extended to borrowers as a part of the Covid-19 relief package supported the lower slippage rate in Q1 FY2021. However, the asset quality pressure could rise in the coming quarters as once the moratorium is lifted. A sizeable share (35% of the loan book in value terms) of CBI's loan book was under moratorium as on August 31, 2020. This leads to significant uncertainty regarding the asset quality in the near term.

In addition to this, CBI had sizeable special mention account (SMA)[3] exposures with SMA 1 and SMA 2 totalling ~5-6% of the standard advances as on March 31, 2020, which are not eligible for restructuring as per the Covid-19 relief package. Though the SMA status of the accounts was corrected in Q1 FY2021 supported by part repayments during the moratorium, ICRA expects that the slippages and restructuring volumes could remain high at 3-4% and 7-8%, respectively, in FY2021. This could constrain the bank's ability to exit the PCA framework in FY2021 unless supported by a large capital infusion.

With NNPAs at 6.76% as on June 30, 2020 and other stressed assets, its solvency[4] profile remains weak with net stressed assets/core capital of 73.96% as on June 30, 2020, though it has improved from past levels of more than 100% as on March 31, 2019).

Profitability and return metrics remain weak – Supported by the reducing cost of funds and the improving share of interest-earning assets, the gross interest spread and the net interest margins (NIMs), as a percentage of average total assets (ATA), improved to 2.24% in FY2020 (against 2.08% in FY2019) even though this was slightly lower than the PSB average of 2.38%. The bank's cost-to-income ratio remained high at 68.71% of ATA for FY2020 because of capital constraints and the declining loan book. As a result, the core operating profitability was 0.93% of ATA for FY202, lower than the PSBs' average of 1.47%.

With high slippages, the credit costs in FY2018 and FY2019 continued to exceed the operating profits, resulting in net losses. The bank reported a net loss of Rs. 1,121 crore (return on asset (RoA) of -0.33%) in FY2020 compared to a net loss of Rs. 5,641 crore (RoA of -1.73%) in FY2019. Unless supported by huge recoveries from legacy stressed assets, ICRA expects the NNPAs to remain above 7% while the credit costs could remain elevated at ~1.4-1.9% of ATA in FY2021, which could result in further losses and capital erosion. In case of sizeable capital support from the GoI to enable the bank's exit from the PCA framework, the credit costs will be higher than the above estimates.

Large capital requirements to exit PCA framework and grow the loan book – CBI has been consistently reporting losses since FY2016 and the outlook on profitability and hence internally generated capital remains weak. While the GoI has extended sizeable capital support during these years, the bank's capital requirements remain high especially if it were to exit the PCA framework.

With a capital infusion in FY2020, CBI's Tier I capital ratio improved to 9.22% as on June 30, 2020 from 7.58% as on June 30, 2019. In September 2020, the bank raised equity of Rs. 255 crore by way of a QIP, which could enable it to

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[3] SMA 0, SMA 1 and SMA 2 loans are overdue loans with overdue status of 0-30, 31-60 days and 61-90 days, respectively

[4] (Net stressed assets including NNPAs, net non-performing investments and net security receipts)/Core equity capital

meet the Tier I of 9.5% as on September 30, 2020 as the slippages are expected to remain low in Q2 FY2021 as well.

ICRA estimates CBI's capital requirement at Rs. 4,200 crore if it has to exit the PCA framework in the current financial year and bring the Net NPA below 6%. However, the capital requirements are estimated to be lower at Rs. 1,700 crore if the bank remains under the PCA framework and maintains its Tier I above 9.5%. In a stress case of slippages, ICRA expects that CBI is likely to maintain a CRAR of 9% even without any further capital infusion in the current year.

Liquidity position: Strong

Supported by a high statutory liquidity ratio (SLR) of 35% of the net demand and time liabilities (NDTL) as on March 31, 2020, which was above the regulatory requirement of 18%, the bank's daily average liquidity coverage ratio (LCR) remained strong at 312% in FY2020 against the regulatory requirement of 100%. The LCR remained strong at 377% in Q1 FY2021. A high level of surplus Government securities, which can be sold to generate liquidity, also drives the positive cumulative mismatches in the 1-year bucket. CBI can also avail liquidity support from the Reserve Bank of India (RBI; through reverse repo against excess SLR investments and the marginal standing facility scheme) in case of urgent liquidity needs.

Rating sensitivities

Positive triggers – ICRA could revise the outlook to Stable and/or upgrade the ratings if CBI's solvency level improves, with net stressed assets/core capital of <60%, while maintaining the NNPAs below 6% and the capital ratios (including CCBs) above the regulatory level on a sustained basis.

Negative triggers – ICRA could downgrade the ratings in case of insufficient capital support from the GoI, leading to sustained capital breaches with a CRAR of <9.0%.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA Rating Methodology for Banks Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group Support	The ratings factor in Central Bank of India's sovereign ownership and the demonstrated track record of capital infusion by the GoI. ICRA expects the GoI to support the bank with capital infusions, if required.
Consolidation	To arrive at the ratings, ICRA has considered the standalone financials of Central Bank of India. However, in line with ICRA's limited consolidation approach, the capital requirement of the Group's key subsidiaries, going forward, has been factored in.

About the company

Central Bank of India was incorporated in 1911. It was nationalised in 1969, along with 13 other major banks of India, by the GoI. Headquartered in Mumbai, CBI is a public sector bank (PSB) with the GoI holding a stake of 89.78% as on September 30, 2020. CBI is the 8th largest PSB with a market share of 2.5% in advances and 3.4% in deposits as on June 30, 2020. Its market share has been declining over the last few years (3.4% in advances and 3.6% in deposits as on March 31, 2015) because of its weak financial position.

For the year ended March 31, 2020, CBI reported a loss after tax of Rs. 1,121 crore on a total asset base of Rs. 3.53 lakh crore compared to a loss after tax of Rs. 5,641 crore on a total asset base of Rs. 3.28 lakh crore for the year ended March 31, 2019. The net profit and total asset base stood at Rs. 135 crore and Rs. 3.61 lakh crore, respectively, as on June 30, 2020. The CRAR was 11.72% (Tier I: 9.33%) as on March 31, 2020 (9.61% and 7.49%, respectively, as on March 31, 2019). The CRAR stood at 11.50% (Tier I: 9.22%) as on June 30, 2020. The bank remains under the PCA framework with NNPAs of 6.76% as on June 30, 2020.

Key financial indicators

Particulars	FY2019	FY2020	Q1 FY2020	Q4 FY2020	Q1 FY2021
Net interest income	6,772	7,629	1,790	1,926	2,145
Profit before tax	(8,170)	(909)	70	(1,661)	316
Profit after tax	(5,641)	(1,121)	118	(1,529)	135
Net advances – Rs. lakh crore	1.47	1.51	1.43	1.51	1.55
Total assets – Rs. lakh crore	3.28	3.53	3.27	3.53	3.61
% CET/Tier I	7.49%	9.33%	7.58%	9.33%	9.22%
% CRAR	9.61%	11.72%	9.58%	11.72%	11.50%
% Net interest margin/ATA	2.08%	2.24%	2.19%	2.22%	2.40%
% Net profit/ATA	-1.73%	-0.33%	0.14%	-1.76%	0.15%
% Return on net worth	-36.48%	-6.49%	2.93%	-31.87%	2.92%
% Gross NPAs	19.31%	18.93%	19.95%	18.93%	18.11%
% Net NPAs	7.73%	7.63%	7.98%	7.63%	6.76%
% PCR (excl TWO)	64.97%	64.61%	65.24%	64.61%	67.23%
% Net NPA/Core equity	102.11%	82.27%	104.13%	82.27%	73.96%

**Total assets and net worth exclude revaluation reserves*
Source: Central Bank, ICRA estimates

All calculations as per ICRA estimates

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years				
		Type	Amount Rated	Amount Outstanding	Rating	FY2020	FY2019			FY2018
					23-Oct-2020	26-09-19	30-11-18	07-08-18	07-05-18	08-08-17
1	Lower Tier II Bonds	Long Term	500.00	500.00	[ICRA] A+ (Negative)	[ICRA] A+ (Negative)	[ICRA] A+ (Negative)	[ICRA] A+ (Negative)	[ICRA] A+ (Negative)	[ICRA] A+ (Negative)
2	Upper Tier II Bonds	Long Term	0.00	-	-	[ICRA] A+ (Negative); withdrawn	[ICRA] A- &	[ICRA] A- &	[ICRA] A- (Negative)	[ICRA] A- (Negative)
3	Upper Tier II Bonds	Long Term	0.00	-	-	[ICRA] A+ (Negative); withdrawn	[ICRA] A- &	[ICRA] A- &	[ICRA] A- (Negative)	[ICRA] A- (Negative)
4	Upper Tier II Bonds	Long Term	0.00	-	[ICRA] A- (Negative); withdrawn	[ICRA] A- (Negative)	[ICRA] A- (Negative)	[ICRA] A- (Negative)	[ICRA] A- (Negative)	[ICRA] A- (Negative)
5	Upper Tier II Bonds	Long Term	0.00	-	[ICRA] A- (Negative); withdrawn	[ICRA] A- (Negative)	[ICRA] A- (Negative)	[ICRA] A- (Negative)	[ICRA] A- (Negative)	[ICRA] A- (Negative)
6	Basel III Tier II Bonds	Long Term	2,000.00	500.00^	[ICRA]A+ (hyb) (Negative)	[ICRA]A+ (hyb) (Negative)	-	-	-	-
	Total		**2,500.00**	**2,000.00**						

Amount in Rs. crore
^ Balance Yet to be placed
Source: ICRA

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

Annexure-1: Instrument details

Instrument	ISIN	Issue Date	Call option	Coupon Rate	Maturity Date	Rated Amount	Current Rating & Outlook
Lower Tier II	INE483A09245	21-Dec-11	No	9.33% p.a.	21-Dec-26	500.00	[ICRA]A+ (Negative)
Upper Tier II	INE483A09211	20-Jan-10	Yes	8.63% p.a. [Step up of 50 bps from 11th year - 9.13% till maturity]	20-Jan-25	500.00	[ICRA]A- (Negative); reaffirmed and withdrawn
Upper Tier II	INE483A09229	11-Jun-10	Yes	8.57% p.a. [Step up of 50 bps from 11th year - 9.07% till maturity]	11-Jun-25	1,000.00	[ICRA]A- (Negative); reaffirmed and withdrawn
Basel III Tier II	INE483A08023	30-Sep-19	No	9.80% p.a.	30-Nov-2029	500.00	[ICRA]A+(hyb) (Negative)
Basel III Tier II	Unplaced	-	-	-	-	1,500.00	[ICRA]A+(hyb) (Negative)
Total						**2,500.00**	

Source: Central Bank of India

Key features of rated instruments

The servicing of the Basel II Lower Tier II Bonds is not subject to any capital ratios and profitability. However, the Basel III Tier II Bonds are expected to absorb losses once the point of non-viability (PONV) trigger is invoked. 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 loss severity vis-à-vis conventional debt instruments. The rated Tier II bonds are expected to absorb losses once the PONV trigger is invoked.

Annexure 2: List of entities considered for limited consolidation analysis

S. No.	Name of the entity	Ownership	Consolidation Approach
1.	Cent Bank Home Finance Limited	64.40%	Limited Consolidation
2.	Centbank Financial Services Limited	100.00%	Limited Consolidation
3.	Uttar Bihar Gramin Bank, Muzaffarpur	35.00%	Limited Consolidation
4.	Uttarbanga Kshetriya Gramin Bank	35.00%	Limited Consolidation
5.	Indo Zambia Bank Limited	20.00%	Limited Consolidation

Source: Central Bank of India, ICRA

Analyst Contacts

Mr. Karthik Srinivasan
+91 22 6114 3444
karthiks@icraindia.com

Mr. Anil Gupta
+91 124 4545 314
anilg@icraindia.com

Ms. Samiksha Karnavat
+91 22 6114 3471
samiksha.karnavat@icraindia.com

Mr. Aashay Choksey
+91 22 6114 3430
aashay.choksey@icraindia.com

Relationship Contact

Mr. L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
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Ahmedabad	+ (91 79) 2658 4924/5049/2008
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