

## RATING RATIONALE

17 Mar 2020

### Dhanlaxmi Bank Ltd

## Brickwork Ratings upgrades its rating on Dhanlaxmi Bank's Basel III Tier II Bonds to 'BWR BB+'

### Particulars:

Instruments	Amount (Rs. Crs.)		Tenure	Rating*	
	Previous	Present		Previous (March, 2019)	Present
Basel III Tier II Bonds (Series XV-B)	150	150	Long Term	BWR BB (Stable)	BWR BB+ (Stable) Upgraded
Lower tier II Bonds (Series X-B) (under Basel II)	14.20	0	Long Term	BWR BB (Stable)	Withdrawn on due redemption
Lower tier II Bonds (Series XI-B) (under Basel II)	3.70	0	Long Term	BWR BB (Stable)	Withdrawn on due redemption
Lower tier II Bonds (Series XIII-B) (under Basel II)	5.00	0	Long Term	BWR BB (Stable)	Withdrawn on due redemption
<b>Total</b>	<b>172.90</b>	<b>150</b>	<b>Rupees One Hundred Fifty Crores Only</b>		

\*Please refer to BWR website [www.brickworkratings.com/](http://www.brickworkratings.com/) for definition of the ratings

\*\* ISIN wise details is provided in Annexure-I&II

### RATING ACTION / OUTLOOK

Brickwork Ratings (BWR) upgrades its rating of Basel III Tier II bonds of Dhanlaxmi Bank, as tabulated above. BWR has also withdrawn its rating for the Basel II Lower Tier II bond issues of the bank amounting to Rs.22.90 Cr.

BWR factors in the bank's performance for FY19 and upto Q3/ 9MFY20, publicly available information, and information and clarification provided by the bank's management.

The rating upgrade for Dhanlaxmi Bank's Basel III Tier II Bonds factors in the bank's comfortable capitalisation, steady balance sheet growth and stable resource profile. The company has maintained total capital adequacy ratios (CAR) and Tier 1 CAR of over 13% and 10%,

respectively over the past three fiscals with a comfortable Basel III leverage of 5.08% and adequate Liquidity Coverage Ratio (LCR) of 320% as of 31 December 2019, which is well above the regulatory requirements of 3.5% and 100%, respectively. The bank's total advances also witnessed robust growth of over 10% year-on-year (y-o-y) in the current fiscal to Rs.6,878 as on 31 December 2019, majorly supported by an increase in advances to corporates and gold loans. Current & Saving accounts (CASA) deposits were also stable at ~30% for the past two fiscals.

The rating however, remains constrained by the concerns on asset quality and profitability. The bank's gross non-performing assets (NPAs) at 7.1% as on 31 December 2019 remains comparatively higher than peers in the industry. Additionally, while the bank has reported net profits for 9MFY20 after reporting net loss in 9MFY19, profitability remains modest.

During FY20, the bank has redeemed Lower Tier II Bonds under Basel II aggregating to Rs.22.90 Cr, and the debenture trustee has confirmed its due redemption. BWR **withdraws** the ratings on these Lower Tier II Bond issues under Basel II amounting to Rs.22.90 Crores.

## **KEY RATING DRIVERS**

### **Credit Strengths:**

**Growth in Business:** The bank is gradually increasing its business. The bank's business has increased to Rs.17,691 Cr (FY19: Rs.17,239 Cr). The deposits have increased to Rs.10,813 Cr (FY19: Rs.10,603 Cr) and advances to Rs.6,878 Cr (FY19: Rs.6,636 Cr). The CASA ratio is maintained at 32%, and retail deposits have also marginally increased from 52% to 54%; for FY20, the bank has grown its exposure to gold loans and corporates. The bank's major advances are from Retail and Corporates, followed by Gold loans, SME and Agri/Micro. The bank has increased its advances to corporates to Rs.1994 Cr (FY19: Rs.1807 Cr), gold loans to Rs.1199 Cr (FY19: 1031 Cr) and Agri & Micro to Rs.759 Cr (FY19: Rs.669 Cr), but decreased advances in SME to Rs.1070 Cr (FY19: 1166 Cr) and Retail to Rs.1856 Cr (FY19: Rs.1963 Cr).

**Comfortable Capitalisation:** On capital adequacy ratios, since FY18, the bank has maintained its total CAR above 13% and Tier 1 CAR ratio above 10%. The bank's net worth had increased to Rs.824 Cr as of 31 December 2019 from Rs.733 Cr as of 31 March 2019. Going forward, the bank endeavours to continue its increase in business mainly from gold loans and selectively from SME, while recording steady growth in other segments. While the bank continues to grow its balance sheet, its ability to manage asset quality, improve profitability and thereby strengthen the capital position will remain a key monitorable.

## Credit Risks:

**Concerns on asset quality:** The bank's gross NPA of 7.1% as of 31 December 2019 is comparatively higher than peers in the industry. Considering the present scale of the bank's business, higher slippages, especially from corporates, may substantially impact its asset quality.

**Modest profitability:** The bank has reported modest profit after tax of Rs.63 Cr for 9MFY20. The bank's increased operating profit for 9MFY20 of Rs.122 Cr (FY19: Rs.95 Cr) is on account of a higher non-interest income amounting to Rs.75 Cr (FY19: Rs.53 Cr), resulting from recoveries from written-off accounts and profit on the sale of investment, which could be non-recurring in nature. The bank's cost to income ratio, despite having improved to 66.3% in 9MFY20 (FY19: 76.2%), is high amongst peers in the industry. The bank's provisioning coverage ratio (excluding write-offs) was at 79% as on 31 December 2019.

## ANALYTICAL APPROACH AND APPLICABLE RATING CRITERIA

For arriving at its ratings, BWR has applied its rating methodology as detailed in the Rating Criteria detailed below (hyperlinks provided at the end of this rationale).

Basel III-compliant bonds are subject to guidelines/regulations of the Reserve Bank of India (RBI) and as detailed in the term sheet of respective issues. BWR considers them as highly complex instruments in terms of published criteria. BWR has rated Basel III instruments; however, restrictions by the regulator on coupon servicing on any of the outstanding bonds due to the non-meeting of regulatory guidelines shall be a key rating sensitivity.

## RATING SENSITIVITIES

The rating sensitivities factor in the bank's performance and business size, apart from the experienced board and management, internal controls and systems, and adherence to the prudence norms of regulatory compliance and corporate governance. The bank has an additional director from the RBI on its board.

**Positive:** Profitable balance sheet growth, an improvement in asset quality and maintaining the current levels of capital adequacy ratios would be the key positives to improve the company's ratings and/or outlook.

**Negative:** Substantial deterioration in the asset quality impacting profitability and capital adequacy constitute negatives that will impact the company's ratings and/or outlook.

## **LIQUIDITY INDICATORS : ADEQUATE**

The bank had adequate liquidity with an average daily LCR of 320% as of 31 December 2019, against the regulatory requirement of 100%. The bank had cash and cash equivalents of Rs.867 Cr and investments of Rs.3783 Cr as of 31 December 2019. The bank's Basel III leverage ratio of 5.08% is well above the regulatory requirement of 3.5%.

## **KEY COVENANTS OF THE INSTRUMENT/FACILITY RATED**

Basel III Tier II Bonds: Basel III Bonds of this nature are susceptible to loss absorbency features as per the terms of the issue and RBI's extant guidelines. The key distinguishing feature of these bonds is the existence of the Point of Non-Viability (PONV) trigger and occurrence of such a PONV trigger event may at the option of the RBI be temporarily or permanently written-off, resulting in permanent loss of the principal to the investor and a default on the instrument to the investor. Basel III Tier II bonds are redeemable after 7 years from the deemed date of allotment with coupon servicing at annual intervals. The bonds are subject to the extant guidelines of the RBI applicable to Tier II Basel III-compliant bonds issued by banks.

## **BANK'S PROFILE**

Background: Dhanlaxmi Bank Ltd (DLB) was incorporated in 1927 in Thrissur, Kerala. Traditionally, the bank has a long-standing relationship with a large number of temple trusts in Southern India, which has given it a better deposit base. As of 31 December 2019, the bank had 247 branches, 346 ATMs and 17 BCs across 14 states and 1 UT. The South-based bank has a major presence in Kerala (58%) and Tamil Nadu (14%), along with 7% each in Maharashtra and Andhra Pradesh, 5% in Karnataka and 9% in other states.

Management: Shri Sajeev Krishnan is the non-executive chairman of the bank since 23 May 2018. Shri Sunil Gurbaxani has been appointed as the managing director and chief executive officer of the bank for three years effective from 27 February 2020. He replaced Ms. T Latha, who resigned on 30 October 2019 due to personal reasons. The bank also has an experienced board of directors and professional key management personnel.

Dhanlaxmi Bank was among the RBI's Prompt Corrective Action (PCA) framework and was removed from the list by the regulator in February 2019, subject to certain conditions and continuous monitoring. Shri. G. Jagan Mohan has been appointed as additional director by the RBI for two years, effective from 27 February 2020 to 26 February 2022 or until further orders from the RBI.

## KEY FINANCIAL INDICATORS

<b>Dhanlaxmi Bank</b>	<b>Audited</b>	<b>Audited</b>	<b>Audited</b>	<b>Unaudited</b>	<b>Unaudited</b>
<b>Key Parameters</b>	<b>FY 2017</b>	<b>FY 2018</b>	<b>FY 2019</b>	<b>9MFY19</b>	<b>9MFY20</b>
Total Deposits	11,294	10,920	10,603	10,725	10,813
<i>Deposit Growth (in %)</i>		-3.31%	-2.90%		0.82%
Advances	6,446	6,110	6,636	5,928	6,878
<i>Loans Growth</i>		-5.21%	8.61%		16.03%
Total Business	17,740	17,030	17,239	16,653	17,691
<i>Business Growth</i>		-4.00%	1.23%		6.23%
CASA Ratio %	29.44%	30.81%	32.00%	31.00%	30.00%
<b>Profitability Ratios (%)</b>					
RoE	2.1%	-9.9%	1.5%	-2.9%	10.2%
RoA	0.1%	-0.2%	0.1%	-0.2%	0.7%
NIM	2.76%	2.90%	3.00%	2.97%	3.30%
Net Interest Income (NII)	331	346	347	259	288
Non Interest Income	111	102	53	26	75
Operating profits	96	146	95	51	122
Provisions & Contingencies	82	171	83	67	59
PAT	12	-25	12	-16	63
Cost to Income Ratio	78.8%	67.4%	76.2%	82.1%	66.3%
<b>Asset Liability Profile (%)</b>					
Loans/Deposit Ratio	57.1%	56.0%	62.6%	55.3%	63.6%
Gross NPAs to Advances	4.8%	7.4%	7.5%	8.1%	7.1%
Net NPAs to Advances	2.6%	3.2%	2.4%	2.9%	1.6%
Std Restructured as a % of Gross Adv.	0.3%	0.5%	0.7%	0.8%	0.5%
Gross NPA% + Restr (Stressed)	5.1%	7.8%	8.1%	8.9%	7.6%
Provision Coverage Ratio	80.0%	80.0%	84.7%	82.8%	89.3%
<b>CRAR</b>	10.3%	13.9%	13.8%	13.5%	13.6%
<i>Tier I</i>	9.0%	10.6%	10.6%	10.3%	10.4%
<i>CET -I</i>	9.0%	10.6%	10.6%	10.3%	10.4%
<i>Tier II</i>	1.3%	3.3%	3.2%	3.3%	3.2%

**NON-COOPERATION WITH PREVIOUS CREDIT RATING AGENCY IF ANY -nil**

## RATING HISTORY FOR THE PREVIOUS THREE YEARS [including withdrawal and suspended]

S.No	Instrument	Current Rating			Rating History		
		Type (Long Term/ Short Term)	Amount (₹ Crs)	Rating	2019	2018	2017
1	Lower Tier II (Basel II)	Long term	-	Withdrawal on due redemption	BWR BB (Stable) <b>Reaffirmed (₹ 22.90 Cr)</b> (08 Mar 2019)	BWR BB (Stable) <b>Reaffirmed (₹ 117 Cr)</b> (14 Mar 2018)	BBWR BB- to BWR BB (Stable) <b>Revised (₹ 200 Cr)</b> (04 Dec 2017)
2	Basel III Tier 2 Proposed	Long term	150	BWR BB+ (Stable) <b>Upgraded</b>	BWR BB (Stable) <b>Reaffirmed</b> (08 Mar 2019)	BWR BB (Stable) <b>Assigned</b> (14 Mar 2018)	-
<b>Total</b>			<b>150</b>	<b>INR One Hundred Fifty Crores Only</b>			

\*Please refer to BWR website [www.brickworkratings.com/](http://www.brickworkratings.com/) for definition of the ratings

## COMPLEXITY LEVELS OF THE INSTRUMENTS

For more information, visit [www.brickworkratings.com/download/ComplexityLevels.pdf](http://www.brickworkratings.com/download/ComplexityLevels.pdf)

## Hyperlink/Reference to applicable Criteria

- [General Criteria](#)
- [Bank & Financial Institutions](#)
- [Basel III Compliant Instruments](#)

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**Dhanlaxmi Bank**  
**ANNEXURE I**  
**INSTRUMENT DETAILS**

Instrument	Issue Date	Amount Rs. Crs	Interest Rate	Maturity Date	ISIN
Basel III Tier II (Series XV-B)	29-Mar-2018	150	11.00%	29-Mar-2025	INE680A08081
Lower tier II (Series X-B)**	29-May-2012	14.20	11.95%	29-May-2019	INE680A09048
Lower tier II (Series XI-B)**	03-Aug-2012	3.70	11.95%	03-Aug-2019	INE680A09063
Lower tier II (Series XIII-B)**	10-Dec-2012	5.00	11.95%	10-Dec-2019	INE680A08065

**TOTAL INR One Hundred Seventy Two Crores and Ninety Lakhs Only**

**\*\*The Lower Tier II Bonds have been redeemed and the ratings withdrawn for the same**

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