

Ratings

Rating Rationale

December 20, 2019 | Mumbai

Indian Bank

Rating placed on 'Watch Developing'

Rating Action

Rs.600 Crore Tier II Bonds (Under Basel III)	CRISIL AAA (Placed on 'Rating Watch with Developing Implications')
Rs.1000 Crore Infrastructure Bonds	CRISIL AAA (Placed on 'Rating Watch with Developing Implications')
Rs.1000 Crore Tier I Bonds (Under Basel III)	CRISIL AA+ (Placed on 'Rating Watch with Developing Implications')
Rs.1000 Crore Tier II Bonds (Under Basel III)	CRISIL AAA (Placed on 'Rating Watch with Developing Implications')
Rs.500 Crore Upper Tier-II Bonds (under Basel II)	CRISIL AAA (Placed on 'Rating Watch with Developing Implications')
Rs.500 Crore Lower Tier-II Bonds (under Basel II)	CRISIL AAA (Placed on 'Rating Watch with Developing Implications')

1 crore = 10 million

Refer to annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL has placed its rating on the long-term debt instruments of Indian Bank on 'Rating Watch with Developing Implications'.

On August 30, 2019, Ministry of Finance announced a set of reforms for public sector banks (PSBs) including consolidation, capital infusion and measures to enhance governance standards. A key announcement was also the amalgamation of 6 PSBs into 4 anchor PSBs. As part of this announcement, it was proposed to amalgamate Allahabad Bank with Indian Bank. In response to the announcement, CRISIL had published a Credit Bulletin on September 5, 2019 conveying that it will continue to closely monitor developments and engage with various stakeholders, and take appropriate rating action thereafter.

In September 2019, in-principle approval from the Boards of Directors of both the merging banks was received. Later, in November 2019, Alternative Mechanism accorded its in-principal approval for the merger of Allahabad Bank and Indian Bank. Further, CRISIL has had discussions with several of the amalgamating banks and understands that the integration process in terms of branch rationalization, alignment of policies, processes and products, joint training of staff, etc., is already underway. The merger is expected to be completed after receipt of all regulatory approvals.

The ratings on the long-term debt instruments of Indian Bank have now been placed on 'Watch with Developing Implications' as there has been significant progress on the amalgamation including approvals from the Boards of the banks. CRISIL will resolve the rating watch once clarity emerges, post-merger completion, on the merged entity's business and financial profile. CRISIL will monitor for potential integration challenges and any impact on the earnings profile of the merged entity. The asset quality of the merged entity will also be a monitorable.

In terms of pro-forma merged financials, the merged bank would have total assets of Rs 5.4 lakh crore, with gross non-performing assets (NPAs) of 12.7% as on September 30, 2019. Common equity tier I (CET-I), Tier I and overall capital adequacy ratio (CAR) of the merged entity were at 10.5%, 10.7% and 12.9% as on September 30, 2019. On the business side, there are potential synergies stemming from a larger distribution network with deeper penetration in key states and operational efficiencies. The branch network strength of Indian Bank and Allahabad Bank will complement each other and the merged bank will have significant presence in the North, East and South of the country.

The ratings on the debt instruments of Indian Bank will continue to factor in the expectation of strong support from the majority owner, Government of India (GoI), and the bank's strong market position and adequate capitalisation, and expectation of strong support from majority owner, GoI. The ratings also factor in the stress on Indian Bank's asset quality, especially in the corporate portfolio and increase in provisions that would continue to impact profitability.

Analytical Approach

For arriving at the ratings, CRISIL has combined the business and financial risk profile of Indian Bank and its subsidiaries and associates. This is because of majority shareholding, business and financial linkages and shared brand. The ratings on Indian Bank's debt instruments continue to factor in strong support that the bank is expected to receive from GoI. This is because GoI is both the majority shareholder in public sector banks (PSBs) and the guardian of India's financial system. The stability of the banking sector is of prime importance to GoI, given the criticality of the sector to the economy, the strong public perception of sovereign backing for PSBs, and the severe implications of any PSB failure in terms of political fallout, systemic stability, and investor confidence in public sector institutions.

Please refer Annexure - List of entities consolidated, which captures the list of entities considered and their analytical treatment of consolidation.

Key Rating Drivers & Detailed Description

Strengths:

* Strong expectation of support from the government

In its ratings on public sector banks (PSBs), CRISIL continues to factor in the strong support of the government, which is both the majority shareholder and guardian of India's financial system. Stability of the banking sector is of prime importance to the government, given the criticality of the sector to the economy, strong public perception of sovereign backing for PSBs, and severe implications of failure of any PSB in terms of political fallout, systemic stability, and investor confidence in public sector institutions. Majority ownership

creates a moral obligation on the government to support PSBs, including Indian Bank. As part of the 'Indradhanush' framework, the government has pledged to infuse at least Rs 70,000 crore in PSBs between fiscals 2015 and 2019, of which Rs 25,000 crore each was infused in fiscals 2016 and 2017.

Furthermore, in October 2017, the government had outlined recapitalisation package of Rs 2.11 lakh crores over fiscals 2018 and 2019, out of which PSBs received around Rs 88,139 crore from the government in fiscal 2018. Government will continue to provide distress support to all PSBs and will not allow any of them to fail; it will also support them to meet Basel III capital regulations. Gol infused around Rs 2500 crore in Indian Bank in fiscal 2020 (pending allotment of equity shares).

*** Strong capitalisation:**

Indian Bank's capitalisation remained comfortable, with CET 1 and Tier-I capital adequacy ratio (CAR) at 10.96% and 11.29% as on March 31, 2019 (11.00% and 11.33% respectively as on March 31, 2018). For the first half ending September 30, 2019, the CET 1, tier 1 and CAR stood at 12.38%, 12.69% and 14.52% respectively. The bank has flexibility to raise additional equity from the market, with Gol stake at 79.62% as on September 30, 2019. Gol's infused capital of Rs 280 crore in fiscal 2015 and Rs 2500 crore in Indian Bank in fiscal 2020 (pending allotment of equity shares).

The capital profile has also been supported by continued internal accruals; Indian Bank is among the few PSBs that have remained profitable in the past couple of years. Indian Bank's strong capitalisation provides cushion against asset-side risks. Its networth coverage for net non-performing assets (NPAs) was around 3.47 times as on September 30, 2019 (2.45 times as on March 31, 2019).

*** Comfortable resource profile:**

Indian Bank's resource profile remains comfortable, with the proportion of low-cost current account and savings account (CASA) deposits at 33.8% as on September 30, 2019 as compared to 35.3% a year earlier. The proportion of highly stable retail deposits (retail term deposits and savings account deposits), at 72.09% of total deposits as on September 30, 2019, supports the resource profile. This is underpinned by its sizeable branch network in the rural and semi-urban areas (54% of total branches as on September 30, 2019).

Weaknesses:

*** Modest asset quality:**

Indian Bank has modest asset quality with gross non-performing assets (NPAs) of 7.2% as on September 30, 2019 compared to 7.1% as on March 31, 2019 (7.37% as on March 31, 2018). The net NPA ratio stood at 3.54% as on September 30, 2019 as against 3.75% as on March 31, 2019 (3.81% as on March 31, 2018). While NPAs have increased in recent years, they remain better than PSB average. Slippages to net opening advances were around 1.96% (annualized) in the first half fiscal 2020 as compared to 4.04% for fiscal 2019. While CRISIL expects some deterioration in the asset quality metrics going forward, the pace of slippages is expected to be lower. This is because large slippages are expected to be limited going forward as the unrecognized stress in the corporate portfolio is low. Ability to recover from large accounts and manage asset quality in the sizeable small and medium enterprise portfolio will be determinant of the asset quality over the medium term.

*** Geographic concentration in operations:**

Tamil Nadu accounted for about 40% of the bank's advances as on September 30, 2019. While the bank is focused on expansion outside Tamil Nadu, the state will continue to account for a sizeable proportion of its business. Hence, Indian Bank's credit risk profile will remain susceptible to changes in the economic and business environment in Tamil Nadu.

Liquidity Superior

The bank has adequate liquidity, supported by a sizeable retail deposit base that forms a significant part of the total deposits. Liquidity coverage ratio was 271.45% as on September 30, 2019, against the regulatory requirement of 100% from January 1, 2019. The excess statutory liquidity ratio was Rs 7079.47 crore (2.89%) as on that date. The bank's liquidity also benefits from access to systemic sources of funds such as the liquidity adjustment facility from the Reserve Bank of India, access to the call money market, and refinance limits from sources such as National Housing Bank and National Bank for Agriculture and Rural Development.

Rating Sensitivity factors

Downward Factors:

* Higher than expected deterioration in asset quality thereby impacting earnings profile

* Decline in capital adequacy ratios below minimum regulatory requirements (including CCB, which is Tier I of 9.5% and overall CAR of 11.5% as on March 31, 2020)

About the Bank

Set up in 1907, Indian Bank is a medium-sized bank. In 2007, it made its initial public offering, resulting in dilution of Gol's ownership to 80%. Gol's ownership stood at 79.62% as on September 30, 2019. The bank had 2887 branches, including 3 overseas branches (one each in Singapore, Colombo, and Jaffna), as on September 30, 2019.

In fiscal 2019, the bank's profit after tax (PAT) was Rs 322 crore on a total income (net of interest expense) of Rs 8901 crore, against a PAT of Rs 1259 crore and a total income Rs 8669 crore the previous fiscal.

For first half of fiscal 2020, the bank reported profit after tax (PAT) of Rs 723.9 crore on total income (net of interest expenses) of Rs 5080.7 crore as against a PAT of Rs 359.4 crore in total income (net of interest expenses) of Rs 4406 crore recorded same period last year.

Key Financial Indicators

As on September 30,	Unit	2019	2018
Total Assets	Rs. Cr.	297662	261643
Total income (net of interest expenses)	Rs. Cr.	5,080	4,406
Profit after tax	Rs Crore	724	359
Gross NPA	%	7.2	7.2
Overall capital adequacy ratio	%	14.5	12.73
Return on assets (annualized)	%	0.5	0.3

Any other information: Not applicable

Note on complexity levels of the rated instrument:

CRISIL complexity levels are assigned to various types of financial instruments. The CRISIL complexity levels are available on

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The distinguishing features of non-equity Tier-I capital instruments (under Basel III) are the existence of coupon discretion at all times, high capital thresholds for likely coupon non-payment, and principal write-down (on breach of a pre-specified trigger). These features increase the risk attributes of non-equity Tier-I instruments, over those of Tier-II instruments under Basel III, and capital instruments under Basel II. To factor in these risks, CRISIL notches down the rating on these instruments from the bank's corporate credit rating. The rating on the Tier-I Bonds (under Basel III) has, therefore, been lowered by one notch from Indian Bank's corporate credit rating, to 'CRISIL AA+' in line with CRISIL's criteria (refer to 'CRISIL's rating criteria for Basel III-compliant instruments of banks').

The factors that could trigger a default event for non-equity Tier-I capital instruments (under Basel III) resulting in non-payment of coupon include: i) the bank exercising coupon discretion; ii) inadequacy of eligible reserves to honour coupon payment if the bank reports losses or low profits; or iii) the bank breaching the minimum regulatory Common Equity Tier-1 (CET I; including Capital Conservation Buffer) ratio. Moreover, given the additional risk attributes, the rating transition for non-equity Tier-I capital instruments (under Basel III) can potentially be higher than that for Tier-II instruments.

Annexure - Details of Instrument(s)

ISIN	Name of Instrument	Date of Allotment	Coupon Rate (%)	Maturity Date	Issue Size (Rs Cr)	Rating Outstanding with Outlook
NA	Infrastructure Bonds*	NA	NA	NA	1000	CRISIL AAA/Watch Developing
INE562A09055	Bonds (Additional Tier I)	30-Mar-16	11.15	Perpetual	500	CRISIL AA+/Watch Developing
NA	Bonds (Additional Tier I)*	N.A	N.A	N.A	500	CRISIL AA+/Watch Developing
INE562A08016	Bonds (Basel III Compliant Tier II Bonds)	28-July-16	8.1	28-July-26	600	CRISIL AAA/Watch Developing
INE562A08024	Bonds (Basel III Compliant Tier II Bonds)*	30-oct-18	8.90	30-Oct-28	290	CRISIL AAA/Watch Developing
INE562A08032		06-Nov-18	8.85	06-Nov-28	110	CRISIL AAA/Watch Developing
INE562A08040		22-Jan-19	8.53	22-Jan-29	600	CRISIL AAA/Watch Developing
INE562A09048	Upper Tier II Bonds (Basel II)	16-Jul-10	8.67	16-Jul-25	500	CRISIL AAA/Watch Developing
INE562A09030	Lower Tier II Bonds (Basel II)	28-Jun-10	8.53	28-Jun-20	500	CRISIL AAA/Watch Developing

*yet to be issued

Annexure - List of entities consolidated

Entity Consolidated	Extent of Consolidation	Rationale for Consolidation
Ind Bank Housing Ltd	Full	Subsidiary
Indbank Merchant Banking Services Ltd	Full	Subsidiary
Tamil Nadu Grama Bank	Partial	Associate
Saptagiri Grameena Bank	Partial	Associate
Puduvai Bharathiar Grama Bank	Partial	Associate

Annexure - Rating History for last 3 Years

Instrument	Type	Current		2019 (History)		2018		2017		2016		Start of 2016
		Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Infrastructure Bonds	LT	0.00 20-12-19	CRISIL AAA/(Watch) Developing	05-09-19	CRISIL AAA/Stable	31-12-18	CRISIL AAA/Stable	06-11-17	CRISIL AAA/Stable		--	--
						30-11-18	CRISIL AAA/Stable					
Lower Tier-II Bonds (under Basel II)	LT	500.00 20-12-19	CRISIL AAA/(Watch) Developing	05-09-19	CRISIL AAA/Stable	31-12-18	CRISIL AAA/Stable	06-11-17	CRISIL AAA/Stable	10-03-16	CRISIL AAA/Negative	CRISIL AAA/Stable
						30-11-18	CRISIL AAA/Stable	08-05-17	CRISIL AAA/Stable	02-03-16	CRISIL AAA/Negative	
								31-03-17	CRISIL AAA/Stable			
Tier I Bonds (Under Basel III)	LT	500.00 20-12-19	CRISIL AA+/(Watch) Developing	05-09-19	CRISIL AA+/Stable	31-12-18	CRISIL AA+/Stable	06-11-17	CRISIL AA+/Stable	10-03-16	CRISIL AA/Negative	--
						30-11-18	CRISIL AA+/Stable	08-05-17	CRISIL AA+/Stable	02-03-16	CRISIL AA/Negative	
								31-03-17	CRISIL AA/Stable			
Tier II Bonds (Under Basel III)	LT	1600.00 20-12-19	CRISIL AAA/(Watch) Developing	05-09-19	CRISIL AAA/Stable	31-12-18	CRISIL AAA/Stable	06-11-17	CRISIL AAA/Stable	10-03-16	CRISIL AAA/Negative	CRISIL AAA/Stable
						30-11-18	CRISIL AAA/Stable	08-05-17	CRISIL AAA/Stable	02-03-16	CRISIL AAA/Negative	
								31-03-17	CRISIL AAA/Stable			
Upper Tier-II Bonds (under Basel II)	LT	500.00 20-12-19	CRISIL AAA/(Watch) Developing	05-09-19	CRISIL AAA/Stable	31-12-18	CRISIL AAA/Stable	06-11-17	CRISIL AAA/Stable	10-03-16	CRISIL AAA/Negative	CRISIL AAA/Stable
						30-11-18	CRISIL AAA/Stable	08-05-17	CRISIL AAA/Stable	02-03-16	CRISIL AAA/Negative	

							AAA/Stable		AAA/Stable		AAA/Negative	
								31-03-17	CRISIL AAA/Stable			

All amounts are in Rs.Cr.

Links to related criteria

[Rating Criteria for Banks and Financial Institutions](#)

[CRISILs Criteria for Consolidation](#)

[Criteria for Notching up Stand Alone Ratings of Entities Based on Government Support](#)

[Rating Criteria for Hybrid Capital instruments issued by banks under Basel II guidelines](#)

[Rating criteria for Basel III - compliant non-equity capital instruments](#)

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