Ujjivan Small Finance Bank Limited (Revised)

July 05, 2022

Ratings

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term Bank Facilities	500.00	CARE A+; Stable (Single A Plus; Outlook: Stable)	Reaffirmed
Total Bank Facilities	**500.00 (₹ Five Hundred Crore Only)**		
Subordinated Non-Convertible Debentures	500.00	CARE A+; Stable (Single A Plus; Outlook: Stable)	Assigned
Total Long Term Instruments	**500.00 (₹ Five Hundred Crore Only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The rating assigned to the instruments/bank facilities of Ujjivan Small Finance Bank Limited (USFB) continues to derive strength from bank's experienced promoter group with seasoned management, improving resource profile of the bank with improvement in deposit funding with increase in CASA & retail deposit share, inheritance of geographically well-diversified loan portfolio from Ujjivan Financial Services Limited (UFSL). The rating takes note of the moderation in capital adequacy levels during FY22. The rating continues to remain constrained by lack of diversity in income profile with unsecured MFI portfolio continuing to constitute 68% of loan portfolio as on March 31, 2022. Ratings also remain constrained due to exposure to inherent risk associated with marginal borrower profile of customers with majority of USFB's customers being from the economically weaker section and low-income segments. Such segments of borrowers are vulnerable to economic downturns as witnessed in sharp decline in collection efficiencies during the COVID-19 affected period leading to sharp moderation in asset quality parameters post COVID. However, CARE takes note of the improvement in collection efficiency from July 2021 and reduction in bank's stressed assets post peaking in September 2021 quarter.

Rating Sensitivities

Positive Factors - Factors that could lead to positive rating action/upgrade:

- Scale up of its business with sustained diversification in secured asset class while improving asset quality on a reasonably seasoned portfolio.

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Delay in ramp up in collections to pre-pandemic levels.
- Material deterioration in asset quality impacting earnings profile of the bank.

Detailed description of the key rating drivers

Key Rating Strengths

Adequate capital headroom albeit moderation in FY22: USFB had shored up its capital levels since its Initial Public Offering (IPO) in December 2019. However, on account of high losses reported and growth in advances during FY22, the Capital Adequacy Ratio (CAR) and Tier 1 CAR Ratio moderated to 18.99% and 17.70% as on March 31, 2022 as against 26.44% and 25.07% respectively as on March 31, 2021. Bank has taken Board approval to raise upto Rs.600 crore via QIP in order to increase the minimum public shareholding in the bank from 16% to 25%. Additionally, bank has board approval in place to raise upto Rs.1500 crore of by way of issuance of non-convertible debt securities.

Improving deposit funding: USFB's reliance on non-deposit funding has exhibited a steady decline in the last couple of years. Deposits as a percentage of total liabilities has increased to 87.9% in FY22 (FYE21: 76.5%) and credit deposit ratio improved to 99.3% as on March 31, 2022 (March 31, 2021: 115.26%). Additionally, low-cost CASA deposits gradually rose to 27.30% as on March 31, 2022 (March 31, 2021: 20.55%). The granularity of the deposit base too reflected an improvement with retail deposits now constituting 54% of the total deposits at FYE22 (FYE21: 48%). CARE Ratings understand that the bank has increased its range of deposit products to widen its customer base.

Geographically Well-diversified Loan Portfolio: USFB has full-fledged banking branches of 575 as on March 31, 2022. USFB's gross loan portfolio stood at Rs.18,162 crore on March 31, 2022 spread across 24 states and UTs with active customer

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

base of 64.8 lakhs (FY21: 59.2 lakhs). Top five states of Karnataka, West Bengal, Tamil Nadu, Maharashtra, and Gujarat contributed to 60.3% of the overall portfolio as of March 2022 (61.5% of the overall portfolio as on March 31, 2021) with top state Tamil Nadu contributing to 15.5% of loan portfolio as of March 2022.

Experienced promoter group with seasoned management: The present senior management team of USFB is highly experienced in financial sector. Mr. Ittira Davis is the current Managing Director (MD) and Chief Executive Officer (CEO) who replaced Mr. Nitin Chugh w.e.f. January 14, 2022. Mr.Ittira Davis has experience of over 40 years in banking industry. USFB's Board comprises of nine directors which includes MD, three Non-Executive directors and five Independent Directors with diverse experience, who bring valuable expertise to the Bank. Bank's operations are ably supported by the senior management team.

Key Rating Weaknesses

Earnings under pressure led by high provisioning; however recovery in profitability witnessed in Q4FY22: Profitability during FY22 was affected by high credit costs. Pre-Provision Operating Profit (PPOP) also decreased by 26.26% during FY22 to Rs. 590.5 crore on account of interest reversals. Albeit decline in cost of funds from 6.93% in FY21 to 5.70% in FY22, bank's Net Interest Margin witnessed decline from 8.91% in FY21 to 8.06% in FY22 owing to decline in yield on advances from 18.22% in FY21 to 16.73% in FY22 with about 68.58% of disbursements made during H2FY22. Further bank also made interest income reversal during the year on account of higher NPA. Bank's operational efficiency also witnessed moderation with cost to income ratio of the bank increasing from 60.57% in FY21 to 71.70% in FY22. Additionally, the credit cost also stood high at Rs.1118 crore during FY22 as against Rs.790 crore during FY21 on account of provisioning made by the bank for the restructuring and slippages during the year. Consequently, the bank reported net loss of Rs.415 crore in FY22 as against net profit of Rs.8.3 crore in FY21. However, the Bank's profitability has witnessed recovery during Q4FY22 and reported PAT of Rs.127 crore. Going forward, Bank's ability to improve asset quality and limiting credit cost thereby protecting earnings would be a key rating monitorable.

Moderation in asset quality post-COVID; significant reduction in stressed asset position post peaking in Q2FY22: Asset quality performance was impacted by the COVID-19 led pandemic with GNPA peaking at 11.80% on September 30, 2021 from 7.07% on March 31, 2021 and gross stressed assets stood at 19.23% as on September 30, 2021. USFB had ramped up its collection efforts and collections witnessed improvement from the month of July 2021 with collections above 100% (including arrears). Consequently, GNPA levels have witnessed improvement to 7.34% as on March 31, 2022 and with rundown of restructured advances, gross stressed assets also declined to 9.69% as on March 31, 2022. Further, with high provisioning made during FY22 the bank's net NPA stood lower at 0.61% as on March 31, 2022 (March 31, 2021: 2.93%). Bank's provision coverage stood high at 92.24% as on March 31, 2022 compared to 60.34% as on March 31, 2021.The total amount of restructured accounts outstanding as on March 31, 2022 stood at Rs.845 crore (4.65% of gross advances).

Exposure to inherent socio-economic and geo-political risks of the microfinance sector: Increase in the non-MFI portfolio has led to a steady reduction in the composition of microfinance loan portfolio. Presently the non-MFI portfolio majorly comprises of housing loan segment (15.1% of the total loan portfolio), loans to MSE segment (9.4% of total loan portfolio) and loans to financial institution (FIG) segments (4.7%) as on March 31, 2022. However, microfinance still comprises a larger share of the loan book at 68.0% as on March 31, 2022 (FY21: 71.8%) which exposes the bank to the inherent risks associated with the industry. The borrower base remains vulnerable to economic downturns and political events which affects their repayment capacity. CARE Ratings understands that the bank will be eventually able to manage the resultant risk as the growth in the non-MFI portfolio gains traction. However, near term risks will be closely monitored.

Liquidity: Adequate

According to the bank's structural liquidity statement (SLS) as on March 31, 2021, liquidity profile is comfortable with no cumulative negative mismatches in any of the time buckets. The liquidity coverage ratio of bank remained comfortable at 152% for quarter ended March 31, 2022 as against the regulatory requirement of 100%. Bank has excess SLR of Rs. 2153 crore as on June 15, 2022. Liquidity is also supported by the refinance lines available to it from SIDBI & NABARD and through sale of PSL certificate to other banks which are short of PSL targets.

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning 'Outlook' and 'Credit Watch' to Credit Ratings
CARE's Policy on Default Recognition
Financial Ratios-Financial Sector
CARE's Rating Methodology for Banks

About the Company

USFB, incorporated on July 04, 2016 is a subsidiary of Ujjivan Financial Services Limited (UFSL). UFSL was a Bangalore based Microfinance Company registered as NBFC-MFI with RBI. It has been in microfinance lending since 2005 and has operated through joint liability group (JLG) model in urban and semi urban areas and target customers who are salaried as well as self-employed women. UFSL was one of the ten entities to be granted "in-principle" approval by Reserve Bank of India (RBI) on September 16, 2015 to set up a bank under the "Guidelines for Licensing of Small Finance Banks in the private sector" (Guidelines) issued by the RBI on November 27, 2014. Subsequently, on November 11, 2016 RBI granted the license to USFB to carry out the banking business in India. Accordingly, USFB formally commenced its operations on February 1, 2017 whereby in line with the terms with Business Transfer Agreement (BTA) effective from February 1, 2017 entered between UFSL and USFB, the entire assets/liabilities of UFSL had been transferred to USFB. As per the listing norms requirement of RBI for SFBs, Bank concluded its IPO process and got listed on NSE and BSE on December 12, 2019. Post IPO, UFSL's shareholding stands at 83.32% in USFB. As on March 31, 2022, the bank has a branch network of 575 branches and has 492 biometric ATMs. The bank has presence across 24 States and Union Territories of India, and with an overall portfolio of around Rs.18,162 crore as on March 31, 2022.

Brief Financials (Rs. crore)	31-03-2020 (A)	31-03-2021 (A)	FY22 (Prov)
Total operating income	3026	3117	3126
PAT	350	8	-415
Total Assets	18411	20380	23604
Net NPA (%)	0.20	2.93	0.61
ROTA (%)	2.18	0.04	-1.89

A: Audited; Prov: Provisional

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated for this company: Annexure 4

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based-Long Term	-	-	-	-	500.00	CARE A+; Stable
Debentures-Non Convertible Debentures	Proposed	Proposed	Proposed	Proposed	500.00	CARE A+; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based - LT-Term Loan	LT	-	-	-	-	1)Withdrawn (07-Jul-20)	1)CARE A+; Stable (03-Jul-19)
2	Debentures-Non Convertible Debentures	LT	-	-	-	-	-	1)Withdrawn (30-Aug-19) 2)CARE A+; Stable (03-Jul-19)
3	Fund-based-Long Term	LT	500.00	CARE A+; Stable	1)CARE A+; Stable (01-Apr-22)	1)CARE A+; Stable (05-Aug-21)	1)CARE A+; Stable (07-Jul-20)	1)CARE A+; Stable (03-Jul-19)

4	Debentures-Non Convertible Debentures	LT	-	-	-	-	-	1)Withdrawn (03-Jul-19)
5	Debentures-Non Convertible Debentures	LT	500.00	CARE A+; Stable				

*Long Term / Short Term

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities

Name of the Instrument	Detailed explanation
A. Financial covenants	
I. CAR	Maintain a minimum CAR of 15%.
II. Tier-I CAR	Maintain a minimum Tier-I CAR of 7.5%.

Annexure 4: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1	Debentures-Non Convertible Debentures	Complex
2	Fund-based-Long Term	Simple

Annexure 5: Bank Lender Details for this Company

To view the lender wise details of bank facilities please click here

Note on complexity levels of the rated instrument: CARE Ratings Ltd. has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About CARE Ratings Limited:
Established in 1993, CARE Ratings Ltd. is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India (SEBI), it has also been acknowledged as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). With an equitable position in the Indian capital market, CARE Ratings Limited provides a wide array of credit rating services that help corporates to raise capital and enable investors to make informed decisions backed by knowledge and assessment provided by the company.
With an established track record of rating companies over almost three decades, we follow a robust and transparent rating process that leverages our domain and analytical expertise backed by the methodologies congruent with the international best practices. CARE Ratings Limited has had a pivotal role to play in developing bank debt and capital market instruments including CPs, corporate bonds and debentures, and structured credit.

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