Indian Overseas Bank

March 08, 2022

Rating

Facilities/Instruments	Amount (Rs. crore)	Rating[1]	Rating Action
Tier-II Bond (Basel-III)	800	**CARE AA-; Stable (Double A Minus; Outlook: Stable)**	**Assigned**
Total Long-term Instruments	**800 (Rs. Eight hundred crore only)**		

Details of instruments/facilities in Annexure-1

Tier-II Bonds under Basel-III are characterised by a 'Point of Non-Viability' (PONV) trigger due to which the Investor may suffer loss of principal. PONV will be determined by the Reserve Bank of India (RBI) and is a point at which the bank may no longer remain a going concern on its own unless appropriate measures are taken to revive its operations, and thus, enable it to continue as a going concern. In addition, the difficulties faced by a bank should be such that these are likely to result in financial losses and raising the Common Equity Tier-I capital of the bank should be considered as the most appropriate way to prevent the bank from turning non-viable.

Detailed Rationale & Key Rating Drivers

The rating assigned to the Tier-II Bond (Basel-III) of Indian Overseas Bank (IOB) factors-in the majority ownership by the Government of India (GoI) and demonstrated funding support by GoI, including the equity infusion of Rs.4,100 crore in the month of March 2021. The rating also factors-in the long track record of operations with strong presence in South India, diversified advances book and deposit base with comfortable CASA. IOB's asset quality metrics have witnessed improvement in the last four years ended March 2021 with significant write-off of NPAs, which resulted in the bank reporting high losses during FY18-FY20. Notwithstanding such losses, IOB reported continuous improvements in its CAR levels during FY18-FY21. The aggregate equity infusion by GoI during the same period stood at Rs.19,974 crore. CARE Ratings expects continuation of the strong support by the GoI.

The rating is constrained by moderate asset quality despite improvement seen over the past few years, and the bank's earnings profile has been moderate as it has started reporting profits in FY21 and 9mFY21; however, the level of profit continues to be moderate and any further impact on account of COVID-19-related stress may impact the asset quality and profitability, going forward.

Rating Sensitivities

Positive Factors - Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Improved profitability on a sustained basis, with ROTA of above 1.00% on a sustained basis.
- Improved asset quality parameters, with net stressed assets/tangible net worth below 25% on a sustained basis.

Negative Factors - Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Significant change in GoI support or shareholding.
- Deterioration in asset quality, with net NPA of 5% or more on a sustained basis.

Detailed description of the key rating drivers

Key Rating Strengths

Majority ownership and support by GoI

IOB's credit profile majorly derives strength from GoI ownership and the demonstrated support from GoI in terms of capital infusion, management and governance. CARE Ratings expects GoI to continue its support to the bank.

The GoI has been supporting public sector banks with regular capital infusions and taking steps to improve capitalisation and asset quality. During FY16 and FY21, the bank has raised equity to the tune of Rs.28,359 crore, of which Rs.27,634 crore is infused by the GoI. With the continuous equity infusion, the shareholding of GoI has increased from 73.80% as on March 31, 2015 to 96.38% as on December 31, 2021.

Diversified advances profile with relatively high growth in retail advance in the past

During FY21, IOB reported a growth in gross advances of 3.58%, with advances growing from Rs.1,34,772 crore as on March 31, 2020 to Rs.1,39,596 crore as on March 31, 2021. The growth during FY21 is majorly driven by the Retail, Agri and MSME (RAM) segment and the share of the same improved to 68.88% as on March 31, 2021 from 62.92% as on March 31, 2020. Notably, the share of RAM in total advances stood at 49% as on March 31, 2016. Over the years, with conscious efforts of the bank to reduce exposure to the corporate loan segment, the share of RAM has witnessed relatively high growth.

The retail loan portfolio has reported a growth of 12.40% during FY21 and the growth is majorly contributed by home loans. Over the past two years, the bank has been reducing the education loan portfolio because of the increase in NPA levels. As on December 31, 2021, the share of RAM, corporate and overseas advance stood at 67.30%, 25.12% and 7.58%, respectively.

As on March 31, 2021, the top 20 individual borrowers constituted about 152% of net worth and 16.05% of gross advances. That said, notably, most of the top borrowers were government-owned entities.

During FY21, the bank had taken conscious efforts to restrict the corporate portfolio/o and fresh limits or enhancements were considered for select accounts, and mostly in highly-rated corporates or accounts guaranteed by state governments.

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

Strong deposit base with comfortable CASA proportion
The deposit base of IOB has been steadily growing for the last four years ended March 31, 2021, with a CAGR of 3.26%, and it reported a higher growth of 7.78% during FY21, with deposits growing from Rs.2,22,952 crore as on March 31, 2020 to Rs.2,40,288 crore as on March 31, 2021. During 9mFY22, it further grew by 2.84% to Rs.2,47,119 crore, as on December 31, 2021.
Over the past few years, IOB has consistently improved the share of CASA, from 28.72% as on March 31, 2016 to 42.52% as on March 31, 2021. As on December 31, 2021, the share of CASA stood at 42.53%. Also, bulk term deposits improved from 26.24% as on March 31, 2016 to 3.35% as on March 31, 2021. However, the sustenance of CASA at present levels remains to be seen.

Improvement in capitalisation levels post equity infusion of Rs.4,100 crore during FY21
With the continuous equity infusion by the GoI, the capital adequacy ratios were above regulatory requirement for the first time in March 31, 2021 over the last five years. The bank does not have any Additional Tier-I Bond (AT-I). So, CET-I and Tier-I CAR remained the same and stood at 12.91% as on March 31, 2021 as against 8.21% as on March 31, 2020. The overall CAR stood at 15.32% as on March 31, 2021 as against 10.72% as on March 31, 2020.
RBI had mandated banks to maintain CET-I, Tier-I and total CAR at 8.00%, 9.50% and 11.50%, respectively, by October 01, 2021. Despite the increase in regulatory requirement because of implementation of the last tranche of capital conservation buffer (CCB), CAR ratios were comfortably higher than the regulatory requirement.
Notably, the bank was placed under prompt corrective action during October 2015, considering the high net NPA and loss reported during FY15. During September 2021, the bank was out of PCA framework, post the improvement in financial and credit profile during FY21. After the bank was placed into the PCA framework, it has been continuously raising equity, majorly from the GoI, to bring back capital adequacy levels above the regulatory requirement.

Key rating Weaknesses
Moderate asset quality parameters
With the continuous higher slippage of 9.11% during FY17 and 13.83% during FY18, GNPA reached a maximum of 25.29% as on March 31, 2018. With the higher recovery and write-offs, GNPA improved on a y-o-y basis to 11.69% as on March 31, 2021 (PY:14.78%), and it further improved to 10.40% as on December 31, 2021. Notably, the bank has written-off portfolios amounting to Rs.31,108 crore and sold portfolios to Asset Reconstruction Company (ARC) amounting to Rs.4,339 crore during FY18 to FY20 (three years). The improvement during FY21 is partly because of the moratorium (March 2020 to August 2020) and restructuring benefits provided by IOB in line with the RBI guidelines. The provision coverage ratio (excluding technical write-off) has improved to 70.02% as on March 31, 2021 and further to 76.75% as on December 31, 2021 from the level of 32.43% as on March 31, 2016. With the improving provision coverage and GNPA, NNPA improved from the peak level of 15.33% as on March 31, 2018 to 3.58% as on March 31, 2021, and further to 2.63% as on December 31, 2021. Notably, despite significant improvement in asset quality reported over the past three years, asset quality parameters continue to remain moderate.
As on March 31, 2021, IOB had security receipts and standard restructured advances outstanding of Rs.2,565 crore and Rs.2,464 crore, respectively. Including the same, gross restructured assets stood at 15.30% as on March 31, 2021, as against 17.87% as on March 31, 2020. Net stressed assets/net worth stood at 65.24%, as on March 31, 2021. As on December 31, 2021, GNPA of the corporate segment remained the highest and stood at 16.73%; notably, the top 20 NPA accounts amounted for 75.10% of the GNPA.

Moderate profitability levels despite improvement in FY21 and 9mFY22
During FY21, IOB reported a PAT of Rs.831 crore on a total income of Rs.22,525 crore as against a loss of Rs.8,527 crore on a total income of Rs.20,766 crore during FY20.
Over the last five years ended March 31, 2021, the NIM of IOB has remained stable and was in the range of 2.00% to 2.55%. During FY21, the NIM stood at 2.23% (PY: 2.10). The opex to average total assets stood at 2.10% during FY21 as against 2.03% during FY20; while cost to income ratio stood at 48.54% in FY21 as against 59.21% in FY20. With the improvement in asset quality during FY21, credit cost declined to 1.91% during FY21 from 4.70% during FY20. With the reduction in credit cost, the company reported a ROTA of 0.31% during FY21 as against a loss during FY20. Notably, the profitability is majorly supported by the increase in profit-on-sale of investments during FY21. The relatively lower profitability of IOB is partly due to the lower credit to deposit ratio (CD ratio). The CD ratio moderated over the last five years to 53.15% as on March 31, 2021 from 71.65% as on March 31, 2016, as the bank was focussing on asset quality instead of loan book growth.
During 9mFY22, IOB reported a PAT of Rs.1,157 crore on a total income of Rs.15,914 crore, as against a PAT of Rs.482 crore on a total income of Rs.16,451 crore during 9mFY21. NIM and ROTA (Annualised) during 9mFY22 stood at 1.67% and 0.56%, respectively, as against 1.71% and 0.25%, respectively, during 9mFY21.

Impact of COVID-19
In trend with the banking industry, slippage during FY21 improved in comparison with the prior years, majorly because of the moratorium provided during March 2020 and August 2020 and the resolution benefits offered.
IOB has restructured the portfolio under Resolution Framework 1.0 and 2.0, amounting to Rs.1,932 crore (1.38% of gross advances) and Rs.5,307 crore (3.58% of gross advances), respectively, and majority of the restructuring is done in the MSME and retail segments. Notably, housing loan and education loans majorly constitute the restructured portfolio in the retail segment.

Liquidity: Strong
As per the structural liquidity statement (ALM) of the bank as on December 31, 2021, the bank has no negative cumulative mismatches across all its time buckets upto six months. As on December 31, 2021, IOB has excess SLR holdings to the tune of Rs.17,726 crore, which is 39.71% higher than the requirement. The LCR, as on December 31, 2021, stood at 182.50% as against the minimum regulatory requirement of 100%.

Analytical approach: Standalone; factoring-in the expected support from the GoI.

Applicable Criteria
Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology – Banks
Financial ratios – Financial sector
Criteria for Rating Basel III - Hybrid Capital Instruments issued by Banks
Factoring Linkages Government Support

About the Bank
The Indian Overseas Bank (IOB) was founded by Mr M. Ct. M. Chidambaram Chettiyar during 1937 and was nationalised by the Government of India during 1969. Currently, IOB is one of the 12 public sector banks (PSB) in India. As on December 31, 2021, GoI held 96.38% in IOB, followed by institutional investors, public and others.
As on December 31, 2021, IOB was operating in India through 3,214 branches, 3,270 ATMs and 2,709 business correspondence (BC) relationships. The bank also has presence in overseas countries through four countries - Singapore, Hong Kong, Colombo and Bangkok. As on December 31, 2021, IOB has a total business (deposits + advances) of Rs.3,95,435 crore through its domestic (3,214 branches) and overseas presence (four countries).
IOB has two joint ventures - Universal Sompo General Insurance Company Limited (USGI), with equity participation of 18% and Indian International Bank (Malaysia), Berhad, with equity participation of 35%. In addition, the bank is also a sponsor for RRB Odisha Gramya Bank (35% shareholding).

Brief Financials (Rs. Crore)	FY20 (A)	FY21 (A)	9mFY22 (Prov.)
Total Operating Income	20,766	22,525	15,914
PAT	-8,527	831	1,157
Total Assets	2,58,395	2,71,790	2,79,237
Net NPA (%)	5.44	3.58	2.63
ROTA (%)	-3.37	0.31	0.56

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

Complexity level of various instruments: Please refer Annexure-3

Covenants of rated instrument / facility: Please refer Annexure-4

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Bonds-Tier II Bonds	Proposed	-	-	-	800.00	CARE AA-; Stable

Annexure-2: Rating history of last three years

Sr. No.	Name of the Instrument/ Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1	Bonds-Tier I Bonds	LT	-	-	-	-	-	1)Withdrawn (28-Jun-18)
2	Bonds-Tier II Bonds	LT	800.00	CARE AA-; Stable				

Annexure-3: Complexity level of various instruments rated for this company

Sr. No	Name of instrument	Complexity level
1	Bonds-Tier II Bonds	Simple

Annexure-4: Detailed explanation of covenants of the rated instrument/facilities: Not Applicable

Note on complexity levels of the rated instrument: *CARE Ratings Limited 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.*

Contact us

Media Contact
Name: Mradul Mishra
Contact no.: 022-6837 4424
Email ID: mradul.mishra@careedge.in

Analyst Contact - 1
Name: Sudhakar P
Contact no.: 044-2850 1003
Email ID: p.sudhakar@careedge.in

Analyst Contact - 2
Name: Ravi Shankar R
Contact no.: 044-2850 1016
Email ID: ravi.s@careedge.in

Relationship Contact
Name: Pradeep Kumar V
Contact no.: 044-2850 1000
Email ID: pradeep.kumar@careedge.in

About CARE Ratings:
CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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