Indian Overseas Bank

December 16, 2022

Ratings

Facilities	Amount (₹ crore)	Rating[1]	Rating Action
Tier-II Bond (Basel-III)	665.00 (800.00)	CARE AA-; Stable (Double A Minus; Outlook: Stable)	Reaffirmed
Tier-II Bond (Basel-III)	1000.00	CARE AA-; Stable (Double A Minus; Outlook: Stable)	Assigned
Total long-term instruments	**1665.00** **(₹ One thousand six hundred and sixty-five 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 a loss of principal. The 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 the most appropriate way to prevent the bank from turning nonviable.

Detailed rationale and key rating drivers

The ratings assigned to the Tier-II Bond (Basel-III) of Indian Overseas Bank (IOB) continue to factor in the majority ownership by the Government of India (GoI) and the demonstrated funding support by the GoI. CARE Ratings Limited (CARE Ratings) expects a continuation of the strong support by the GoI. The ratings also factor in the long track record of operations with a strong presence in South India, the comfortable capitalisation levels, the diversified advances book and deposit base with a comfortable current account savings account (CASA).

The ratings are constrained by the moderate asset quality despite improvement seen over the past few years, with improvement in the gross non-performing assets (GNPA) and gross stressed asset position. The bank's earnings profile has seen considerable improvement in FY22 as against the earlier years, however, the level of profitability continues to be moderate and any further impact in the asset quality on account of the performance of the stressed assets may impact the profitability, going forward.

Rating sensitivities

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

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

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

- Significant change in the GoI support or shareholding.
- Deterioration in asset quality, with net non-performing assets (NNPA) of 5% or more on a sustained basis.

Detailed description of the key rating drivers

Key rating strengths

Majority ownership and support by the GoI: IOB's credit profile mainly derives strength from the GoI ownership and the demonstrated support from the GoI in terms of capital infusion, management, and governance. CARE Ratings expects the GoI to continue its support to the bank. The GoI has been supporting public sector banks (PSBs) with regular capital infusions and taking steps to improve capitalisation and asset quality. During the period from FY16 (refers to the period April 01 to March 31) to FY21, the bank has raised equity to the tune of ₹28,359 crore, of which ₹27,634 crore is infused by the GoI. With the continuous equity infusion, the shareholding of the GoI has increased from 73.80% as on March 31, 2015, to 96.38% as on September 30, 2022.

Diversified advances profile with a relatively high proportion of retail advance: IOB reported growth in gross advances of 11.6% and 10.8% during FY22 and H1FY23 (refers to the period April 01 to September 30), respectively, with advances growing from ₹139,596 crore as on March 31, 2021, to ₹172,714 crore as on September 30, 2022. The retail, agri, and micro,

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

small and medium enterprises (MSME) (RAM) advances continue to constitute the major portion of advances, forming 65.51% of the advances as on September 30, 2022. The share of corporate advances witnessed a marginal increase from 24.44% as on March 31, 2021, to 26.82% as on September 30, 2022. RAM constituted 23.06%, 24.21%, and 18.24%, respectively, as on September 30, 2022. As on September 30, 2022, the top 20 individual borrowers constituted about 153% of the net worth and 17.94% of the gross advances. That said, notably, most of the top borrowers were government-owned entities and highly rated corporate accounts. CARE Ratings expects the proportion of RAM to remain at similar levels in the medium term.

Strong deposit base with a comfortable CASA proportion: The deposit base of IOB has been steadily growing over the years and it reported a growth of 9.1% during FY22, with deposits growing from ₹2,40,288 crore as on March 31, 2021, to ₹2,62,159 crore as on March 31, 2022. CASA deposits registered a growth of 11.46% during FY22, resulting in a slight increase in the CASA proportion from 42.52% as on March 31, 2021, to 43.44% as on March 31, 2022. The deposit base has remained stable at ₹261,728 crore as on September 30, 2022. The CASA share slightly moderated to 42.76% as on September 30, 2022. Bulk term deposits stood at 4.24% as on September 30, 2022. However, the sustenance of CASA at the present levels remains to be seen.

Comfortable capitalisation levels: The bank was placed under prompt corrective action in October 2015, considering the high NNPA and loss reported during FY15. After the bank was placed into the prompt corrective action (PCA) framework, it has been continuously raising equity, mainly from the GoI, to bring back capital adequacy levels above the regulatory requirement. In September 2021, the bank was moved out of the PCA framework. The capital adequacy ratio (CAR) and Tier-I stood at 13.83% and 10.71%, as on March 31, 2022. The CAR ratios were comfortably higher than the regulatory requirement, with the CAR and Tier-I CAR at 15.14% and 12.11%, respectively, as on September 30, 2022, as against the regulatory requirement of 11.5% and 9.50%, respectively. It is to be noted that the reported CAR levels are after discounting the zero coupon recapitalisation bonds to the net present value. CARE Ratings expects the CAR levels to remain comfortable, as the bank is expected to remain profitable in the medium term in line with the industry.

Key rating weaknesses

Moderate asset quality parameters, albeit an improvement witnessed during FY22 and H1FY23: The bank's asset quality parameters have witnessed improvement during FY22 with the GNPA improving from 11.69% as on March 31, 2021, to 9.82% as on March 31, 2022, and it further improved to 8.53% as on September 30, 2022. It is to be noted that the bank has written off a portfolio amounting to ₹3,769 crore and sold a portfolio to ARC amounting to ₹91 crore during FY22.

Slippages have remained higher at 4.10% during FY22 as against 2.78% during FY21. The lower slippages during FY21 was partly because of the moratorium (March 2020 to August 2020) and restructuring benefits provided by IOB in line with the RBI guidelines. The bank's provision coverage ratio (PCR; including technically written off accounts) also stood healthy at 90.94% as on September 30, 2022. With the improving provision coverage and GNPA and NNPA levels, the bank's gross stressed assets position (GNPA + standard restructured assets + security receipts) as a percentage of the gross advances has also witnessed improvement from 20.08% as on December 31, 2021, to 15.39% as on March 31, 2022, which has further improved to 11.85% as on September 30, 2022. The net stressed assets as a percentage of the net worth stood at 39.17% as on September 30, 2022 (81.48% as on December 31, 2021).

Improvement in profitability levels during FY22 and H1FY23: The bank's net interest margin (NIM) has remained stable at 2.22% in FY22 (FY21: 2.23%). Its net interest income (NII) has witnessed increase to ₹6,311 crore during FY22 as against ₹5,899 during FY21, in line with the increase in the loan portfolio. However, non-interest income witnessed a decline from ₹5,559 crore during FY21 to ₹4,903 crore during FY22. The decline is mainly because of the decrease in profit on sale of investments. The bank's operational efficiency parameters witnessed improvement with opex/average assets of the bank at 1.92% in FY22 compared with 2.10% in FY21. Furthermore, the bank's credit cost also stood lower at 1.40% in FY22 as against 1.91% in FY21 with an improvement in asset quality parameters. Consequently, the bank's ROTA witnessed improvement to 0.60% in FY22 as against 0.31% in FY21. The bank's ability to improve asset quality by limiting credit cost, thereby protecting the earnings profile, will be a key rating monitorable. The relatively lower NIM and profitability of IOB is partly due to the lower credit to deposit ratio (CD ratio). The CD ratio (Net Advances/ Deposits) stood moderate at 55.02% as on March 31, 2022, which has witnessed improvement to 61.92% as on September 30, 2022, aided by healthy loan book growth during H1FY23. During H1FY23, IOB reported a profit-after-tax (PAT) of ₹894 crore on a total income of ₹10,881 crore as against a PAT of ₹703 crore on a total income of ₹10,698 crore during H1FY22. The NIM and ROTA (annualised) during H1FY23 stood at 2.47% and 0.60%, respectively, as against 2.26% and 0.51%, respectively, during H1FY22. CARE Ratings expects the bank to remain profitable in the medium term, with credit costs remaining moderate in line with the industry.

Liquidity: Strong

The liquidity profile of the bank remains strong, with no cumulative negative mismatches in any of the time periods as per the asset and liability management (ALM) statement submitted by the bank as on September 30, 2022. The liquidity coverage ratio of the bank remained comfortable at 169.19% as on September 30, 2022, as against the regulatory requirement of 100%. In addition, the bank had excess statutory liquidity ratio (SLR) investments of ₹20,317 crore as on September 30, 2022 (excess of 43.6% of the SLR requirement).

Analytical approach

Standalone, factoring in the expected support from the GoI.

Applicable criteria

Criteria on Assigning 'Outlook' or 'Credit Watch' to Credit Ratings
Policy on Default Recognition
Financial Ratios-Financial Sector
Notching by Factoring Linkages with Government
Rating Methodology - Banks
Criteria for Rating Basel III - Hybrid Capital Instruments issued by Banks

About the company

IOB was founded by M Ct M Chidambaram Chettiyar in 1937 and was nationalised by the GoI in 1969. Currently, IOB is one of the 12 PSBs in India. As on September 30, 2022, the GoI held 96.38% in IOB, followed by institutional investors, the public, and others. As on September 30, 2022, IOB was operating in India through 3,214 branches, 3,438 ATMs, and 2,228 business correspondence (BC) relationships. The bank also has a presence in overseas countries through four branches, namely, Singapore, Hong Kong, Colombo, and Bangkok. As on September 30, 2022, IOB has a total gross business (deposits + gross advances) of ₹434,441 crore through its domestic (3,214 branches) and overseas presence (four countries).

IOB has two joint ventures (JVs), namely, Universal Sompo General Insurance Company Limited (USGI) with an equity participation of 18% and Indian International Bank (Malaysia), Berhad, with an equity participation of 35%. In addition, the bank is also the sponsor for RRB Odisha Gramya Bank (35% shareholding).

Brief Financials (₹ crore)	**March 31,** 2021 (A)	**March 31,** 2022 (A)	**September 30, 2022** (Prov)
Total income	22,525	21,633	10,881
PAT	831	1,710	894
Total Assets*	271,790	296,628	303,806
Net NPA (%)	3.58	2.65	2.56
ROTA (%)	0.31	0.60	0.60

A: Audited; Prov: Provisional.; *Total Assets adjusted for revaluation reserve.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years: Please refer Annexure-2

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

Complexity level of the 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 (Rs. crore)	Rating Assigned along with Rating Outlook
Bonds-Tier II bonds	INE565A08043	31-03-2022	8.60%	31-03-2032	665.00	CARE AA-; Stable
Bonds-Tier II bonds	Proposed	-	-	-	1000.00	CARE AA-; Stable

Annexure-2: Rating history for the 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.	Bonds-Tier II Bonds	LT	665.00	CARE AA-; Stable	-	1)CARE AA-; Stable (08-Mar-22)	-	-
2.	Bonds-Tier II Bonds	LT	1000.00	CARE AA-; Stable	-	-	-	-

*Long term/short term.

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

Name of the Instrument	Detailed Explanation
A. Financial covenants	NA
B. Non-financial covenants	
I. Call Option	Call option available at the end of five years (with the prior approval of the RBI).

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

Sr. No.	Name of Instrument	Complexity Level
1.	Bonds-Tier II Bonds	Simple

Note on the complexity levels of the rated instruments: CARE Ratings 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.

Annexure-5: Bank lender details for this company

Not applicable

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About us:
Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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