UCO Bank

February 20, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Tier-II bonds (Basel III)[&]	500.00	CARE AA-; Positive	Reaffirmed; Outlook revised from Stable

Details of instruments in Annexure-1.

[&]Tier-II bonds under Basel-III are characterised by a 'point of non-viability' (PONV) trigger by which the investor may suffer a loss of principal. The PONV will be determined by the Reserve Bank of India (RBI) at which the bank may no longer remain a going concern by itself unless appropriate measures are taken to revive operations, enabling it to continue as a going concern. Difficulties faced by a bank should be such that these are likely to result in financial losses and raising the Common Equity Tier-I (CET I) capital should be considered the most appropriate way to prevent it from turning non-viable.

Rationale and key rating drivers

Rating assigned to debt instrument of UCO Bank (UCO) continues to factor in majority ownership by Government of India (GoI), its demonstrated support by multiple equity infusions in the past and expected continued support in future. The rating continues to derive strength from improved capitalisation levels, diversified advances book with an established franchise largely in northern and eastern India and improving profitability.

The rating continues to be constrained by moderate-but-improving asset quality parameters, moderate resource profile with lower-than-average proportion of current account savings account (CASA) deposits as compared to peer banks and relatively smaller size with geographical concentration.

Rating sensitivities: Factors likely to lead to rating actions

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

- Sustaining profitability parameters.
- Significantly improving size of the bank.
- Improving asset quality parameters, with net stressed assets/tangible net worth below 25% on a sustained basis.

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

- Materially diluting GoI shareholding or support.
- Deteriorating asset quality parameters with net NPA ratio of over 5% on a sustained basis.
- Deteriorating profitability resulting in return on total assets (ROTA) of under 0.3% on sustained basis
- Deteriorating capitalisation levels with cushion above minimum regulatory requirement lower than 1% on a sustained basis.

Analytical approach

The rating is based on the bank's standalone profile and factor in strong and continued support from GoI, which has majority shareholding.

Outlook: Positive

Revision in the outlook to 'Positive' reflects CARE Ratings Limited's (Care Ratings) expectation that UCO Bank will continue to sustain improving asset quality and profitability. The bank's profitability levels improved over the last 3 years and the momentum is expected to continue in the medium term. The revision also factors in comfortable capitalisation levels, aiding growth going forward. The outlook will be revised to stable, if the bank is unable to sustain improving asset quality parameters and profitability.

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

Detailed description of the key rating drivers

Key strengths

Majority ownership and expected support from the Government of India (GoI)

GoI continues to be the majority shareholder with 95.39% stake in UCO Bank as on December 31, 2023. GoI has been supporting public sector banks with regular capital infusions and steps to improve capitalisation, operational efficiency, and asset quality. From FY16 onwards, GoI has cumulatively infused equity capital aggregating to ₹22,645 crore, including recapitalisation bonds. Given the majority ownership of GoI, UCO is expected to receive timely and adequate support as capital from GoI and is considered a key rating sensitivity.

Comfortable capitalisation levels

In the past, the bank's capitalisation was supported by multiple equity infusions by the GoI against recapitalisation bonds. The bank has seen improved capitalisation levels in FY23 due improving internal accruals, unwinding discount from zero coupon bonds and reducing deferred tax assets. The bank raised Additional Tier I (AT I) bonds of ₹500 crore in FY23.

UCO reported Common Equity Tier (CET) I ratio of 13.12%, Tier I CAR of 13.53% and capital adequacy ratio (CAR) of 16.01% (16.94% including 9MFY24 profits) as on December 31, 2023, as compared to CET1 and Tier I CAR of 10.97% and CAR of 13.74% as on March 31, 2022.

The bank has not and does not plan to raise any capital in FY24 but has a board approval to raise up to ₹500 crore AT1 bonds and ₹2,000 crore of equity capital for FY24. UCO may resort to raising equity in FY25 to reduce GoI's shareholding. CARE Ratings expects the bank to maintain adequate cushion over minimum regulatory requirement going forward.

Diversified advances profile with growth

The bank saw increase in advances post coming out of the prompt corrective action (PCA) framework of RBI in September 2021. UCO's gross advances increased by 25% in FY23 and 19% (y-o-y) in end of 9MFY24 (refers to April 01 to December 31) with corporate segment reporting higher growth at 33% and 20% respectively whereas non-corporate segment represented by retail, agriculture and MSME (RAM) grew relatively slower at 18% each in both periods. The overseas corporate exposure grew fast and within the domestic corporates, exposures to industries such as NBFC, textiles, metals among others have grown rapidly.

Within retail segment, the bank's focus was more on housing loans for capital conservation and better asset quality. Gross advances stood at ₹1,79,195 crore as on December 31, 2023, with wholesale loans constituting 48% of total advances and RAM segment constituting 52% of total advances. CARE Ratings expects RAM segments, which continues to be the bank's major focus area, and corporate to remain at similar levels in the medium term.

Improvement in earnings but moderate profitability

UCO's earning profile has been improving over the past few years, after growing its advances book supported by lower slippages after coming out of PCA.

The interest income increased by 18% in FY23 as compared to previous year due to 25% growth in advances book and the rise in advance yields. Interest expenses grew faster at 38% due to increasing term deposits and deposit rates resulting in net interest income (NII) to grow by 13%. The bank's net interest margin (NIM) improved marginally to 2.69% for FY23 against 2.61% for the previous year due to increase in systemic interest rates, increasing yields and the cost of deposits. However, non-interest income declined by 19% y-o-y due to treasury loss in FY23 from significant rise in interest rates. The total income of the Bank stood at ₹20,159 crore in FY23 as compared to ₹18,082 crore in FY22 registering a growth of 11%. Employee expenses increased due to provision for wage revision from November 2022 onwards, which resulted in operating expenses to rise by 15%. UCO's Pre-Provisions Operating Profit (PPOP) as a result fell from ₹4,797 crore for FY22 to ₹4,341 crore for FY22. As the bank made higher provisions in FY22 and earlier years, incremental provisions for FY23 were lower, resulting in credit cost to reduce from 1.23% in FY23 to 0.53% in FY22, helping the bank to report improved profit after tax (PAT) of ₹1,862 crore in FY23 with ROTA of 0.63% as compared to net profit of ₹930 crore for FY22, translating to ROTA of 0.37%.

In 9MFY24, the bank continued to see increase in its NII and total income resulting in pre-provision operating profit to increase to ₹3,303 crore as compared to ₹2,984 crore for 9MFY23. The bank's credit cost rose in 9MFY24 due to prudent increase in provisions on standard assets (and includes provision of ₹105 crore related to unrecovered erroneous IMPS credits) resulting reported fall in PAT by 12% at ₹1,128 crore as compared with ₹1,281 crore for 9MFY23. CARE Ratings expects the bank to sustain its profitability levels in the medium term, with credit costs remaining moderate, in line with the industry.

On November 15, 2023, UCO Bank reported that from November 10, 2023, to November 13, 2023 certain transactions initiated in Immediate Payment Service (IMPS), by holders of other banks resulted in credit to UCO account holders without actual receipt of money. UCO has recovered 86% of the total amount (₹705.31 crore of ₹820 crore) that was mistakenly credited to many accounts. UCO has made adequate provision for unrecovered amounts in Q3FY24. The bank is undertaking measures to strengthen its systems.

Key weaknesses

Improving asset quality despite being moderate

Asset quality parameters have seen improvement in the last four years (FY20 onwards) after a deteriorating trend, which started rising from FY16 onwards and peaked in FY19 with Gross NPA ratio of 25%, Net NPA ratio of 9.71% and Net NPA to Net worth ratio of 148.96% as on March 31, 2019, largely from exposure to weaker large-ticket corporate accounts. The Gross NPA declined from FY20 onwards from lower slippages and higher write-offs. The slippage ratio (on net opening advances) improved to 1.75% for FY23 and 1.38% for 9MFY24 as against 5.72% for FY22 and 3.24% for FY21. As a result, the bank was able to bring down Gross NPA ratio significantly to 3.85% as on December 31, 2023. The bank's Net NPA, Provision Coverage Ratio (excluding TWO) and Net NPA to Net worth stood at 0.98%, 75.38% and 10.29% respectively as on December 31, 2023 respectively. The bank held ₹1,335 crore of provisions on standard assets as on December 31, 2023.

The bank's gross stressed assets (GNPA+ Standard restructured assets+ Security Receipts) to gross advances and Net stressed assets to net worth reduced from 12.14% and 75.85% as on March 31, 2022, to 6.55% and 39.53% as on December 31, 2023 (March 31, 2023: 8% and 45.24%) respectively. The bank's special mention accounts (SMA) with delinquencies above 30 days past due (dpd), SMA 1 and SMA 2 stood at 3.28% of gross advances as on December 31, 2023. CARE rating expects asset quality to continue improving from current levels in the medium term.

Moderate resource profile with low CASA deposits

Total deposits of the bank grew at 11.28% from ₹2,24,073 crore as on March 31, 2022, to ₹ 2,49,338 crore as on March 31, 2023 (December 31, 2023: ₹2,56,261 crore). CASA Deposits however grew slower at 3.84% over the previous year falling to 36.79% as on March 31, 2023 (December 31, 2023: 36.27%) as compared to 39.42% for the corresponding date of previous year, relatively lower as compared to peer public sectors banks. Post rate hikes in FY23 and fast credit growth, the entire banking industry witnessed challenge in growing their deposits, especially CASA, with depositors preferring term deposits over savings and with banks placing more reliance on bulk deposits.

As banks are competing for deposits by giving higher interest rates on term deposits and bulk deposits, cost of deposits is increasing. While majority of UCO's deposits were granular with ticket size of less than ₹15 lakh, the proportion of bulk deposits (ticket size of above ₹2 crore) has been increasing since March 2021.

With tightening market liquidity, cost of deposits for the bank may rise slightly from current levels as around 20% to 25% of term deposits that are yet to be repriced. The full impact on cost of deposits would be seen by H1FY25. The bank has excess SLR against which, repo borrowings can be taken to fund its advances instead of reliance on bulk deposits to help the bank reduce the impact of increase in cost.

Relatively moderate size and concentration in East and Northern India

UCO Bank is one of the relatively smaller PSBs with a total business of around ₹4.3 lakh crore and an asset size of ₹3.1 lakh crore with almost, 63% of branches are situated in northern, eastern and north-east part of India as on December 31, 2023.

Liquidity: Adequate

According to Structural Liquidity Statement as on December 31, 2023, there are no negative cumulative mismatches based on the ALM in time buckets up to three months. The bank manages deposit maturities in a particular time bucket by appropriately modifying deposit rates. The bank's average Liquidity Coverage Ratio (LCR) stood at 141% for the quarter ended December 31, 2023, as against regulatory requirement of 100%. Comfort can be drawn from excess Statutory Liquidity Ratio (SLR) amounting to approximately ₹21,344 crore (8.35%) as on December 31, 2023. The bank has access to systemic liquidity such as RBI's LAF and MSF facility and access to refinance from SIDBI, NHB, and NABARD, among others and access to call money markets.

Environment, social, and governance (ESG) risks

Environmental

- As part of green initiative, LED lights have been used in branches and use of one-time plastic at administrative offices have been reduced.
- The bank has launched an Electric Vehicle loan scheme offering to finance purchase of electric car.
- The bank extended credit facility of ₹792.28 crore to the renewable energy sector.

Social

- As a part of CSR, the bank contributed to Chief Minister Relief Fund, Himachal Pradesh for natural calamity restoration.
- More than 11 lakh persons were educated through 35,931 programmes conducted by 106 Center for Financial Literacy (CFL) sponsored by the bank till December 31, 2023.
- Bank Lending to rural women by providing credit to more than 14.41 lakh rural women through over 1.61 lakh Self Help Group Loans.
- The bank implemented Government Sponsored Social Security Scheme through its pan India branches, the details of which (number of beneficiaries) are as under: Pradhan Mantri Suraksha Bima Yojana (PMSBY) – 50.78 lakh, Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) – 22.92 lakh and Atal Pension Yojna (APY) – 10.02 lakh.

Governance

- The bank has grievance redressal policy, citizen charter, and internal ombudsman scheme among others which is also available on its website.
- The bank has Enterprises Fraud Risk Management solution for preventing unauthorised electronic banking transactions.
- The bank has a policy on prevention prohibition and redressal of Sexual Harassment of women at workplace.

Applicable criteria

Policy on default recognition
Factoring Linkages Government Support
Financial Ratios - Financial Sector
Rating Outlook and Credit Watch
Rating Basel III - Hybrid Capital Instruments issued by Banks
Bank

About the company and industry

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Financial services	Financial services	Banks	Public sector bank

UCO Bank, incorporated in 1943, is a Kolkata-based mid-sized public sector bank that operates through a network of domestic 3,217 branches and three international branches as on December 31, 2023, with branch concentration in north and east India. In October 2003, Government of India (GoI) divested 25% stake through an initial public offering (IPO) of equity shares. However, post many capital infusions over subsequent years, GoI shareholding has been steadily increasing and stood at 95.39% as on December 31, 2023. Post the asset quality review (AQR) by RBI, the bank saw significant increase in its NPAs, resulting in having to make provisions, impacting its profitability and capital adequacy.
UCO Bank was put into prompt corrective action (PCA) framework by RBI in May 2017 and was subsequently removed from PCA in September 2021 after it met parameters under the framework. UCO Bank is sponsor of Paschim Banga Gramin Bank (PBGB), a regional rural bank (RRB), headquartered at Howrah, West Bengal with four regional offices and 230 branches as on December 31, 2023.

Brief Financials (₹ crore)	March 31, 2022 (A)	March 31, 2023 (A)	9MFY24 (UA)
Total income	18,082	20,159	18,135
PAT	930	1,862	1,128
Total assets	2,55,832	2,89,851	3,09,206
Net NPA (%)	2.70	1.29	0.98
ROTA (%)	0.37	0.68	0.50

A: Audited; UA: Unaudited. All analytical ratios are according to CARE Ratings' calculations.
Note: 'these are latest available financial results.'

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

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

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

Complexity level of the various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Tier II Bonds – Basel III	INE691A08088	31.03.2022	8.51%	31.03.2032	100	CARE AA-; Positive
Tier II Bonds – Basel III Proposed	-	-	-	-	400	CARE AA-; Positive

Annexure-2: Rating history for 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 2023-2024	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
1	Bonds-Tier II Bonds	LT	500.00	CARE AA-; Positive	-	1)CARE AA-; Stable (23-Feb-23)	1)CARE AA-; Stable (24-Mar-22)	-

* Long term

Annexure-3: Detailed explanation of covenants of rated instruments – Not applicable

Annexure-4: Complexity level of instruments rated

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

Annexure-5: Lender details

Not applicable

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.

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About us:
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