

Utkarsh Small Finance Bank Limited

January 05, 2026

Instruments	Amount (₹ crore)	Rating ¹	Rating Action
Tier-II Bonds	200.00	CARE A; Negative	Reaffirmed; Outlook revised from Stable
Tier-II Bonds	-	-	Withdrawn

Details of instruments in Annexure-1.

Rationale and key rating drivers

CARE Ratings Limited (CareEdge Ratings) has revised the outlook on the long-term rating of Utkarsh Small Finance Bank Limited (USFBL) to Negative from Stable due to sustained stress in its micro-banking portfolio, which accounted for 44% of total advances as on September 30, 2025. The stress led to higher credit costs and interest income reversals in H1FY26 and is likely to keep profitability under pressure in FY26.

USFBL's gross non-performing assets (GNPA) ratio deteriorated significantly in H1FY26 to 12.42% as on September 30, 2025, from 9.43% as on March 31, 2025, and 3.88% as on September 30, 2024, due to elevated slippages following the implementation of the MFIN 2.0 regulatory framework from April 01, 2025 onwards. Consequently, the net NPA (NNPA) to net worth ratio also worsened to 41.10% as on September 30, 2025, compared to 31.67% as on March 31, 2025, and 5.27% as on September 30, 2024.

In response to heightened stress in the micro-banking segment, USFBL has recalibrated its disbursement strategy and pivoted towards secured lending, resulting in moderated overall advances growth in FY25 and H1FY26. As a result of this strategic shift, the share of micro-banking in the advances portfolio declined from 62% as on March 31, 2024, to 44% as on September 30, 2025 (46% including Business Correspondence), while secured loans increased from 34% to 47% in the same period. While this transition is expected to improve portfolio quality in the medium term, it is likely to exert some pressure on profitability due to the relatively lower yields associated with secured lending products.

The bank's ability to contain further slippages, improve collection efficiency, and earnings momentum while strengthening its secured lending base and maintaining adequate capitalisation will be key rating sensitivities going forward.

However, the rating favourably factors in USFBL's adequate capitalisation, supported by an equity infusion of ₹950 crore through a rights issue in November 2025, against the earlier envisaged ₹750 crore. Strengthened capital base provides adequate headroom to absorb near-term asset quality stress.

On the liabilities front, while the bank has successfully expanded its deposit base in recent years with significant growth in deposits improving its credit to deposit ratio, its current account savings account (CASA) ratio remains relatively low at 20.90% as on September 30, 2025. The rating also considers comfortable average liquidity coverage ratio (LCR) of 241% for Q2FY26, providing adequate liquidity cushion.

CareEdge Ratings has withdrawn the rating assigned to tier-II bonds (Basel II; ISIN No. INE735W08020) of USFBL with immediate effect in line with its withdrawal policy, as the bank has redeemed the instrument and there is no amount outstanding against the issue.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors: Factors that could individually or collectively lead to positive rating actions/upgrade:

- Sustained improvement in asset quality and profitability while maintaining comfortable capitalisation levels.
- Improvement in profitability metrics with return on total assets (ROTA) above 1.5% on a sustained basis
- Diversification in resource profile with continuous improvement in CASA proportion on a sustained basis.

¹Complete definition of ratings assigned are available at www.careratings.com and other CARE Ratings Limited's publications.

Negative factors: Factors that could individually or collectively lead to negative rating actions/downgrade:

- Deteriorating capitalisation with overall capital adequacy ratio (CAR) going below 18%.
- Sustained deterioration in asset quality, profitability, and liquidity.

Analytical approach: Standalone

Outlook: Negative

Revision in the outlook reflects continued stress in the microfinance segment, affecting USFBL's asset quality and profitability, which is expected to continue even in H2FY26. The outlook may be revised to stable if the asset quality parameters show sustained improvement, resulting in better profitability, while maintaining healthy capitalisation levels.

Detailed description of key rating drivers:
Key strengths
Adequate capitalisation levels supported by ₹950 crore equity raise

USFBL's capitalisation levels moderated in H1FY26, with the capital adequacy ratio (CAR) touching 17.21% and Tier-I at 14.16% as on September 30, 2025, compared to 20.93% and 17.88%, respectively, as on March 31, 2025, primarily due to continued losses. However, the bank continued to maintain adequate capitalisation, with sufficient cushion over the minimum regulatory requirement of 15% (Tier-I: 7.5%).

The bank's capital position improved following an equity raise of ₹950 crore through a rights issue in November 2025, against the earlier envisaged capital raise of ₹750 crore. The enhanced capital base provides adequate headroom to absorb potential asset quality stress amid the challenging operating environment. CareEdge Ratings expects that the bank will continue to maintain adequate capital buffers over regulatory thresholds amidst the near-term asset quality and profitability pressures.

Continued diversification of loanbook

Advances growth moderated in FY25 and H1FY26, primarily as the bank is calibrating its micro-banking disbursements following stricter regulatory guardrails and sectoral stress while continuing strong growth in non-micro-banking retail segments and improving the advances mix in favour of secured portfolio. The bank registered 2.3% degrowth in the gross loan portfolio year-on-year (y-o-y) and stood at ₹18,655 crore as on September 30, 2025, while the micro-banking segment de-grew by 24%. The largest segment of the portfolio continues to be micro-banking loans; though its share has reported a decline from 62% of the loan book as on March 31, 2024, to 44% as on September 30, 2025 (46% including Business Correspondence). While the bank will continue to grow micro-banking loans, it is focusing on increasing other non-micro banking segments, especially secured loans, whose proportion increased from 34% as on March 31, 2024, to 47% as on September 30, 2025. Going forward, other lending verticals (being smaller in size) are expected to grow even faster than micro-banking business, and hence, the share of micro-banking loans in overall loan book is expected to reduce further. Reduction in microfinance loan book and reduction in the geographical concentration remain a key rating monitorable.

Key weaknesses
Deterioration of asset quality and profitability

USFBL's asset quality deteriorated materially in FY25 and H1FY26, with the GNPA rising to 12.42% as on September 30, 2025 (March 31, 2025: 9.43%, March 31, 2024: 2.51%), and the NNPA to net worth ratio increasing sharply to 41.10% (March 31, 2025: 31.67%, March 31, 2024: 0.16%), which is relatively higher than its peers. This was primarily due to higher slippages in the micro-banking segment, which accounted for a sizable portion of the loan book. As on September 30, 2025, the bank's provision coverage ratio (PCR) on GNPA stood at 63%, which is comparatively lower than that of peer small finance banks. CareEdge Ratings notes that the X-bucket collection efficiency for micro-banking, which improved in Q4FY25 compared to previous quarter, deteriorated in H1FY26 due to implementation of MFIN Guardrail 2.0 from April 01, 2025. In addition to micro-banking, USFBL has also witnessed sequential deterioration in GNPA levels across non-microbanking retail segments, including micro, small and medium enterprise (MSME), housing, commercial vehicle/construction equipment (CV/CE), and other retail loans.

The bank reported net loss of ₹588 crore for H1FY26 compared to profit after tax (PAT) of ₹24 crore in FY25 (FY24: ₹498 crore), affected by high credit costs and interest reversals. Going forward, profitability is likely to remain under pressure in H2FY26, due to continued, despite gradually reducing stress in the microfinance segment and a shift in the product mix towards relatively lower-yielding secured loans. USFBL's operations are expected to remain loss-making for FY26 with some recovery expected in Q4FY26.

Geographical concentration of loan portfolio

The bank has 1,104 banking outlets across 27 states and union territories (UTs) as on September 30, 2025. Top two states - Bihar and Uttar Pradesh, constituted ~46% of its branches and 47% of its gross loan portfolio (over 70% micro-banking loans) as on September 30, 2025. However, geographical concentration is gradually improving with the expansion of the branch network, and majority non-microbanking portfolio is now outside the two states.

The share of micro-banking loans in the loan book remained dominant at 44% as on September 30, 2025 (46% including business correspondence), which exposes the bank to inherent risks associated with the industry such as socio-political intervention, regulatory uncertainties, and challenges of unsecured lending.

Relatively low CASA

The bank's liability mix has undergone substantial change as deposits as a percentage of total liabilities has been increasing with reduction in dependence on borrowings, which is evident from the improving credit to deposit ratio which stood at 79% as on September 30, 2025. USFBL's deposits have grown 10% y-o-y and stood at ₹21,447 crore with CASA proportion remaining relatively modest at 20.90% as on September 30, 2025. The bank's CASA proportion remains lower compared to its peers in the small finance banking industry. The bank has been focusing on building its granular retail deposits book and its CASA plus retail term deposits (up to ₹3 crore) constituted 78% of total deposits as on September 30, 2025. Its dependence on wholesale term deposits has reduced to 22% as on September 30, 2025 (September 30, 2024: 32%). CareEdge Ratings expects the bank to focus on raising CASA deposits, which would provide the bank a stable depositor base and reduce cost of funding in the medium term.

Liquidity: Strong

Per the structural liquidity statement as on September 30, 2025, there were no negative cumulative mismatches for time buckets up to one year. The bank also maintained surplus liquidity of ~₹4,400 crore which provides liquidity buffer. The bank's average LCR remained comfortable at 241% for Q2FY26, while the net stable funding ratio stood at 116% as on September 30, 2025, against the minimum regulatory requirement of 100%. In addition, the bank has access to borrowing from Reserve Bank of India's (RBI's) liquidity adjustment facility (LAF) and marginal standing facility (MSF) and option to refinance from Small Industries Development Bank of India (SIDBI), National Housing Bank (NHB), and National Bank for Agriculture and Rural Development (NABARD) among others, and access to call money markets.

Environment, social, and governance (ESG) risks

Given USFBL's service-oriented nature of business, its direct exposure to environmental risks remains low. However, it faces implicit environmental risks through its portfolio of assets. The bank has targeted reduction in energy consumption, preserve water quality, and availability in addition to plantation of trees. Customer data privacy and security remain the key social risk-related vulnerabilities for USFBL as breaches could attract regulatory attention and damage the bank's reputation. While digital banking offers many benefits to the bank, poor execution of IT strategies and failure to adequately meet customer needs could lead to high costs. On a positive note, USFBL is enhancing financial inclusion by offering products and services aimed at marginalised sections of society, addressing social concerns. Prudent lending to these underserved segments could create growth opportunities, which must be weighed in the context of asset quality risks, including borrower creditworthiness, economic vulnerabilities, and regulatory uncertainties. USFBL's Board comprises seven Directors, of which four are Independent Directors, including two female Directors.

Applicable criteria

[Definition of Default](#)

[Rating Outlook and Rating Watch](#)

[Banks](#)

[Financial Ratios - Financial Sector](#)

[Withdrawal Policy](#)

[Rating Basel III - Hybrid Capital Instruments issued by Banks](#)

About the company and industry

Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Financial services	Financial services	Banks	Other bank

USFBL was incorporated on April 30, 2016, and commenced banking operations on January 23, 2017, pursuant to a small finance bank licence granted by the Reserve Bank of India on November 25, 2016. The bank provides banking and financial services with a focus on microfinance, with lending activities largely concentrated in rural and semi-urban areas, while deposit and other banking services are offered across the country.

USFBL extends microfinance loans under the joint liability group (JLG) model and micro-banking business loans (MBBL), and MSME loans, housing loans, personal loans, CV/CE loans, and wholesale lending. Headquartered in Varanasi, Uttar Pradesh, USFBL is a subsidiary of Utkarsh CoreInvest Limited (UCL), an RBI-registered NBFC-NDSI-CIC with 42.67% stake (post right issue) and 68.92% stake (pre right issue).

As on September 30, 2025, the bank operated through 1,104 banking outlets, 306 ATMs and 778 micro-ATMs, and is led by Govind Singh, MD and CEO, whose reappointment was approved by the RBI on September 21, 2024.

The Boards of USFBL and its holding company, UCL, approved a scheme of amalgamation of UCL with USFBL on September 20, 2024, with a share exchange ratio of 699 USFBL shares for every 100 UCL shares and an appointed date of April 01, 2025, subject to approvals. The bank has received no-objection from the RBI, BSE, and NSE, and filed a joint application with the NCLT, Allahabad Bench on December 26, 2025, to convene stakeholder meetings.

USFBL Financials

Brief Financials (₹ crore)	March 31, 2024 (A)	March 31, 2025 (A)	H1FY26 (UA)
Total income	3,579	4,365	1,956
Profit after tax (PAT)	498	24	-588
Total assets	23,798	28,010	27,267
Net interest margin (NIM) (%)	8.81	7.81	5.44
ROTA (%)	2.32	0.09	-4.25
Gross non-performing assets (NPA) (%)	2.51	9.43	12.42
Net non-performing assets (NPA) (%)	0.03	4.84	5.02
Capital adequacy ratio (CAR) (%)	22.57	20.93	17.21

A: Audited; UA: Unaudited; Note: these are latest available financial results

All calculations per CareEdge Ratings

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Detailed explanation of covenants of rated instrument / facility: Annexure-3

Complexity level of instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Bonds-Tier-II Bonds	INE735W08020	31-Aug-2018	10.58	30-Aug-2025	-	Withdrawn
Bonds-Tier-II Bonds	INE735W08061	27-Nov-2024	10.90	27-Nov-2031	105.00	CARE A; Negative
Bonds-Tier-II Bonds	Proposed	-	-	-	95.00	CARE A; Negative

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 2025-2026	Date(s) and Rating(s) assigned in 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023
1	Bonds-Tier II Bonds	LT	-	-	-	-	-	1)Withdrawn (29-Sep-22)
2	Bonds	LT	-	-	1)CARE A; Stable (13-Aug-25) 2)CARE A+; Negative (12-Jun-25)	1)CARE A+; Stable (31-Oct-24) 2)CARE A+; Stable (24-Sep-24)	1)CARE A+; Stable (26-Sep-23)	1)CARE A; Positive (29-Sep-22)
3	Bonds	LT	200.00	CARE A; Negative	1)CARE A; Stable (13-Aug-25) 2)CARE A+; Negative (12-Jun-25)	1)CARE A+; Stable (31-Oct-24)	-	-

LT: Long term

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

Annexure-4: Complexity level of instruments rated

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

Annexure-5: Lender details: Not applicable

Note on complexity levels of rated instruments: CareEdge Ratings has classified instruments rated by it based on complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for clarifications.

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