# Canara Bank

**November 24, 2021**

**Ratings**

| Instrument | Amount (Rs. crore) | Rating[1] | Rating Action |
|---|---|---|---|
| Tier II Bonds (Basel III)# | 3,000.0 | **CARE AAA; Stable (Triple A; Outlook: Stable)** | **Reaffirmed** |
| Tier II Bonds (Basel III)# | 4,400.0$ | **CARE AAA; Stable (Triple A; Outlook: Stable)** | **Reaffirmed** |
| Additional Tier I Bonds (Basel III)@ | 1,450.0$ | **CARE AA+; Stable (Double A Plus; Outlook: Stable)** | **Revised from CARE AA; Stable (Double A; Outlook: Stable)** |
| **Total** | **8,850.0 (Rs. Eight thousand eight hundred fifty crore only)** | | |

*Details of instruments/facilities in Annexure-1;*
*$Transferred from erstwhile Syndicate Bank pursuant to its amalgamation with Canara Bank.*

*#Tier-II Bonds under Basel III are characterized by a 'Point of Non-Viability' (PONV) trigger due to which the investor may suffer a 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 Common Equity Tier-I capital of the bank should be considered as the most appropriate way to prevent the bank from turning non-viable. In CARE Ratings' opinion, the parameters considered to assess whether a bank will reach the PONV are similar to the parameters considered to assess rating of Tier-II instruments even under Basel II. CARE Ratings has rated the Tier-II bonds under Basel III after factoring in the additional feature of PONV.*
*@CARE Ratings has rated the aforesaid Basel III Compliant Additional Tier-I Bonds after taking into consideration its key features as mentioned below:*

- *The bank has full discretion at all times to cancel coupon payments.*
- *The coupon is to be paid out of current year profits. However, if the current year's profits are not sufficient, i.e., payment of such coupon is likely to result in losses during the current year, the balance of coupon payment may be made out of revenue reserves and/or credit balance in profit and loss account provided the bank meets the minimum regulatory 2 CARE Ratings Limited Press Release requirements for Common Equity Tier I [CET I], Tier I and Total Capital Ratios and capital buffer frameworks as prescribed by the Reserve Bank of India [RBI].*
- *The instrument may be written-down upon CET I breaching the pre-specified trigger of 5.5% before March 31, 2019, and 6.125% on and after October 1, 2021, or written-off / converted into common equity shares on occurrence of the trigger event called point of non-viability (PONV). The PONV trigger shall be determined by RBI. Any delay in payment of interest/principal (as the case may be) due to invocation of any of the features mentioned above would constitute as an event of default as per CARE Ratings' definition of default and as such these instruments may exhibit a somewhat sharper migration of the rating compared with other subordinated debt instruments.*

**Detailed Rationale & Key Rating Drivers**

The ratings assigned to debt instruments of Canara Bank continue to derive strength from majority ownership by Government of India (GoI), its market position as third-largest Public Sector Bank (PSB) as on September 30, 2021, its established retail franchise with strong network in southern states of India and experienced management. The rating strengths are partially offset by relatively low CASA and modest asset quality levels.

As per CARE Ratings' (CARE's) criteria for rating of hybrid instruments issued by banks, CARE has been notching down the Additional Tier I (AT I) Bonds issued by the banks by one to several notches below the Tier II Bond rating depending on the expected adequacy of eligible reserves, cushion over minimum regulatory capital and other credit risk assessment parameters of the individual bank to factor in the additional risk in these instruments on account of several unique features of these instruments including loss absorption features and coupon discretion clause which make them very different from other types of debt instruments.

For public sector banks (PSB), the current ratings factor in government support. The restriction on coupon payment in the event of loss or through distributable reserve may pose challenge in coupon servicing for weaker banks. However, in the past, the GoI, as the majority shareholder, has provided support to PSBs in terms of capital infusion on need basis to not only make the coupon payments but also to call back the bonds.

[1]*Complete definitions of the ratings assigned are available at [www.careratings.com](www.careratings.com) and in other CARE publications.*

Apart from capital support, PSBs have received support from GoI and the regulator in terms of allowing accumulated losses to be set-off against the share premium account which has increased the quantum of distributable reserves available to service the AT I Bonds. GoI also has initiated consolidation of the sector by amalgamation of relatively weaker and smaller banks into larger banks which has seen strengthening of balance sheets of the PSBs. CARE further expects that GoI would provide capital support to PSBs on need basis so that covenants for coupon payment is not breached in future.
In this background, CARE has revised the rating of AT I Bonds of Canara Bank considering the strengthening in overall credit profile of the bank including improvement in capital cushions over minimum regulatory requirement, improvement in profitability and improvement in the distributable reserves position. The revision in the ratings assigned to debt instruments of Canara Bank consider the setting off accumulated loss amounting Rs.18,495.30 crore against share premium reserve in Q2FY22 which improved the amount of distributable reserves available for AT1 coupon payment and the improvement in capitalization levels supported by fresh equity infusion of Rs.2,500 crore in H1FY22 (refers to the period April 1 to September 30).
Rating Sensitivities
*Positive factors-Factors that could lead to positive rating action/upgrade*
- Not Applicable

*Negative factors- Factors that could lead to negative rating action/downgrade*
- Significant slippages impacting earnings profile and deterioration in Net NPA to net worth.
- Deterioration in capitalisation levels on a sustained basis and inability to maintain sufficient cushion over the regulatory capital.

**Detailed description of the key rating drivers**
**Key Rating Strengths**
**Majority ownership by Government of India (GOI) and demonstrated support**
GoI continues to have majority stake in the bank from which CB has received periodical capital infusion and experienced management and the same is expected to continue. As per directive from Ministry of Finance, GOI, Syndicate Bank (SB) has merged with Canara Bank (CB) effective from April 01, 2020. Currently, Canara Bank is the third-largest PSB as on September 30, 2021, increasing the strategic importance of the bank. During the past five fiscals (FY16-FY20 [refers to the period April 1 to March 31]), GOI has infused Rs.20,701 crore on a combined basis in Canara Bank and Syndicate Bank. As part of its recapitalization plan, GOI had infused Rs.6,571 crore during September 2019. GOI is the majority shareholder holding 62.93% stake as on September 30, 2021 (69.33% as on March 31, 2021). During Q3FY21, the bank raised Rs.2,000 crore by way of QIP issue in which LIC was major subscriber. Also, in order to further strengthen its capital position, the bank has raised Rs.2,500 crore by way of QIP issue in Q2FY22.

Merger update:
The bank has completed integration process in terms of policies and processes for services provided to customers and customers of both Canara Bank and erstwhile Syndicate Bank can avail the services from any of the branches of the merged entity. Treasury operations and IT processes have been successfully integrated from April 01, 2020. The bank has reorganized the Regional Offices, Circle Offices and created various Verticals at Head Office to meet the requirement of Amalgamated Bank. The Migration of CBS to upgraded version 11.8 and Peripheral Applications (Internet Banking, Mobile Banking, UPI, CTS, Government Business Modules, etc) was completed in January 2021.

**Established franchise and deposit base with a strong presence in the southern states**
Total business of the bank stood at Rs.17.19 lakh crore as on September 30, 2021, with deposit base of Rs.10.32 lakh crore and advances of Rs.6.86 lakh crore. The bank has an established presence with network of 9,800 branches and 10,988 ATMs as on September 30, 2021. The bank also has four international branches in New York, London, Hong Kong and Dubai.

**Improvement in Profitability levels**
During FY21, the bank reported PAT of Rs.2,557 crore as against loss of Rs.5,838 crore reported in FY20. The improvement in PAT is supported by both increase in net interest income and non-interest income. Supported by relatively higher decrease in cost of deposits, NIM improved to 2.22% in FY21 from 2.01% in FY20. With increase of 40% in non-interest income and relatively stable operating expenses, Canara Bank reported pre-provisioning operating profit (PPOP) of Rs.20,009 crore in FY21 (PY: Rs.12,832 crore in FY20). During FY21, Credit cost improved to 1.61% from 1.85%. The bank made additional provision in FY21 on account of Covid-19, aggregating to Rs.500 crore. Total Provisioning on account of Covid-19 stood at Rs.994 crore (of this Rs.494 crore corresponds to provision related to OTR accounts). The provision coverage ratio (Including technical write-off) stood at around 80%.
During H1FY22, the bank reported PAT of Rs.2,510 crore as against PAT of Rs.851 crore in H1FY21. With decline in interest income, NIM witnessed a marginal decline, however, with higher non-interest income on account of higher treasury profits

and improvement in operating expenses, CB reported higher operating profit of Rs.11,084 crore, thus, translating into a growth of 20.47% (Y-o-Y).

**Capital adequacy improved with fresh Infusion of capital in FY21 and H1FY22**

Canara Bank raised capital in form of AT1 Bonds and Common Equity during FY21 aggregating to Rs.4,936 crore. The bank has raised Equity Capital to the tune of Rs.2,000 crore in Q3FY21 through QIP. CB's CET I, Tier I and Total CAR stood at 8.62%, 10.08% and 13.18% as on March 31, 2021 as against 8.40%, 9.56% and 12.96% as on April 1, 2020. The bank raised additional equity of Rs.2,500 crore during Q2FY22, thus strengthening the capital adequacy. Total CAR stood at 14.37% as on September 30, 2021. Furthermore, the bank has also raised capital aggregating to Rs.1,500 crore in the form of AT1 Bonds in the month of October 2021 which is further expected to strengthen the capital position of the bank. With these the extent of capital cushion available over regulatory minimum has witnessed further improvement in H1FY22.

**Key Rating Weaknesses**

**Improvement in asset quality with relatively more recoveries and reduced slippages**

Bank's asset quality continues to remain moderate albeit improved during FY20 and FY21. Aided by lower net slippages on account of various measures announced by RBI including extension of moratorium and additional credit lines under various schemes, higher amount of recoveries and write-off, the bank's asset quality improved in FY21. With reduction in slippage ratio to 2.35% in FY21 from 4.28% in FY20, bank's Gross NPA ratio improved to 8.93% (PY: 9.39%) and Net NPA ratio improved to 3.82% (PY: 4.34%). In H1FY22, asset quality improved marginally on account of higher recoveries and GNPA and NNPA ratio stood at 8.42% and 3.21% as on September 30, 2021.
The bank has restructured the portfolio, under Covid-19 Resolution Framework 1.0 aggregating to Rs.5,067 crore (0.74% of gross advances) and restructured portfolio aggregating to Rs.13,475 crore under Covid-19 Resolution Framework 2.0 (1.96% of gross advances). Going forward, the ability of the bank to limit incremental slippages or restructuring and maintain asset quality would be critical to the earnings profile of the bank and the same will be a key rating sensitivity.

**Relatively low CASA share but high retail deposit**

Aided by widespread branch network, the bank has witnessed steady growth in the bank's low-cost CASA deposits by 14% YoY to Rs.3.30 lakh crore as on March 31, 2021 from Rs.2.90 lakh crore as on March 31, 2020 (on combined basis) and the bank's share of CASA in domestic deposits improved to 34.33% as on March 31, 2021 from 33.36% as on March 31, 2020. Share of bank retail term deposit (as a percentage of total deposit) stood at 41.58% as on March 31, 2021 (PY: 39.84%). Share of bulk deposits reduced to 21.00% of the total deposits as on March 31, 2021 (24.10% as on March 31, 2020). As on September 30, 2021, deposits stood at Rs.10,32,536 crore (2.14% growth during H1FY22), whereas share of CASA in domestic deposits was maintained at 34.11% as on September 30, 2021.

**Impact of Covid-19**

Impacted by the second wave of Covid-19, In April 2021, Collection Efficiency reduced to 88.8% from 92% in March 2021. The gross stressed assets (GNPA+ Standard Restructured assets+ Security Receipts outstanding) as a percentage of gross advances stood at 10.74% as on March 31, 2021. The bank has restructured around Rs.18,542 crore of portfolio under resolution framework 1.0 and 2.0 (2.70% of gross advances). The bank's ECLGS book stood at Rs.11,044 crore (1.61% of gross advances) as on September 30, 2021. The same is expected to increase the total stressed assets portfolio; however, it remains comparable to its peers.

**Liquidity: Strong**

According to the bank's structural liquidity statement (SLS) as on March 31, 2021, there are no negative cumulative mismatches in up to 1-year maturity bucket. Furthermore, the bank has maintained an excess SLR investment of Rs.103,942 crore as on March 31, 2021. These factors provide cushion to the bank's liquidity profile. CB's liquidity coverage ratio stood at 129.18% for quarter ended March 31, 2021, against the minimum regulatory requirement of 90% (till March 31, 2021). (100% from April 1, 2021). Furthermore, the bank has access to market liquidity support like Liquidity Adjustment Facility (LAF) and Marginal Standing Facility (MSF) from RBI.

**Analytical approach:** Standalone along with expected support from 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 Company**
Canara Bank (CB) is a Bengaluru-based public sector bank which was established in 1906. As per directive from Ministry of Finance, GOI for amalgamation of Syndicate Bank (SB) into Canara Bank the merger has become effective from April 1, 2020. Currently, Canara Bank is the third-largest PSB as on September 30, 2021, increasing the strategic importance of the bank. GOI is the majority shareholder holding 62.93% stake in the bank followed by LIC of India holding 8.83% as on September 30, 2021. As on September 30, 2021, the Bank (on combined basis) had 9,800 branches, of which 3,037 are in rural, 2,796 in semi-urban, 1,971 in urban and 1,996 in metro areas. The bank also has four overseas branches located at New York, London, Hong Kong and Dubai. Mr Lingam Venkata Prabhakar is the MD and CEO, who is assisted by a team of Executive Directors and General Managers heading various departments. As on September 30, 2021, the bank had gross advances of Rs.686,813 crore and deposits of Rs.1,032,536 crore.

| Brief Financials (Rs. crore) | FY20* | FY21 (A) | H1FY22(P) |
|---|---|---|---|
| Total operating income | 81,710 | 84,525 | 42,272 |
| PAT | -5,838 | 2,557 | 2,510 |
| Total Assets | 1,028,429 | 1,134,372 | 1,199,133 |
| Net NPA (%) | 4.34 | 3.82 | 3.21 |
| ROTA (%) | -0.58 | 0.24 | 0.43 |

*A: Audited; P: Provisional *Combined Financials of CB+SB.*
*Note: All Analytical ratios are as per CARE Ratings' calculations.*
*Total Assets exclude deferred tax assets and are net of revaluation reserve*

**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 rated for this company:** Annexure 3

**Annexure-1: Details of Instruments/Facilities**

| Name of the Instrument | ISIN No. | Date of Issuance | Coupon Rate | Maturity Date | Size of the Issue (Rs. crore) | Rating assigned along with Rating Outlook |
|---|---|---|---|---|---|---|
| Tier II Bonds (Basel III)-I | INE476A08076 | March 11, 2020 | 7.18% | March 11, 2030 | 3000.00 | CARE AAA; Stable |
| Bonds- Lower Tier II bonds-II | INE667A09177 | December 31, 2012 | 9.00% | December 31, 2022 | 1000.0 | CARE AAA; Stable |
| Tier II Bonds (Basel III)-II | INE667A08021 | March 23, 2015 | 8.75% | March 23, 2025 | 400.0 | CARE AAA; Stable |
| Tier II Bonds (Basel III)-II | INE667A08013 | December 02, 2014 | 8.95% | December 02, 2024 | 750 | CARE AAA; Stable |
| Tier II Bonds (Basel III)-II | INE667A08039 | September 28, 2015 | 8.58% | September 28, 2025 | 1000.0 | CARE AAA; Stable |
| Tier II Bonds (Basel III)-II | INE667A08047 | December 18, 2015 | 8.62% | December 18, 2025 | 750.0 | CARE AAA; Stable |
| Tier II Bonds (Basel III)-II | INE667A08096 | May 03, 2017 | 8.00% | May 03, 2027 | 500.0 | CARE AAA; Stable |
| Additional Tier I Perpetual Bonds (Basel III)-I | INE667A08088* | October 24, 2016 | 9.95% | Perpetual | 1000.0 | CARE AA+; Stable |
| Additional Tier I Perpetual Bonds (Basel III)-I | INE667A08104 | July 25, 2017 | 9.80% | Perpetual | 450.0 | CARE AA+; Stable |

**Redeemed*

**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 II Bonds | LT | 3000.00 | CARE AAA; Stable | 1)CARE AAA; Stable (03-Aug-21) | 1)CARE AAA; Negative (03-Sep-20) | 1)CARE AAA (CWD) (03-Mar-20) | - |
| 2 | Bonds-Tier II Bonds | LT | 4400.00 | CARE AAA; Stable | 1)CARE AAA; Stable (03-Aug-21) | 1)CARE AAA; Negative (03-Sep-20) | - | - |
| 3 | Bonds-Tier I Bonds | LT | 1450.00 | CARE AA+; Stable | 1)CARE AA; Stable (03-Aug-21) | 1)CARE AA; Negative (03-Sep-20) | - | - |

** Long Term / Short Term*

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

| Basel III Tier-II bonds | Detailed explanation |
|---|---|
| **Non-Financial covenants** | |
| i. Conditions for exercise of call option | On or after the 5th anniversary date from the date of allotment or any anniversary issuer may at its sole discretion, having notified the trustee not less than 21 calendar days prior to date of exercise of such issuer call subject to prior approval of RBI subject to tax call/regulatory call or issuer demonstrates that its capital position is well above the minimum capital requirements after the issuer call is exercised. |

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

| Sr No | Name of instrument | Complexity level |
|---|---|---|
| 1 | Tier II Bonds (Basel III) | Simple |
| 2 | Tier II Bonds (Basel III) | Complex |
| 3 | Lower Tier II | Complex |
| 4 | Tier I Bonds (Basel III) | Complex |

***Note on complexity levels of the rated instrument:*** *CARE Ratings has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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**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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