Bandhan Bank Limited

July 07, 2020

Ratings

Instruments	Amount (Rs. crore)	Ratings[1]	Rating Action
Unsecured Subordinated Non- Convertible Debenture	**160 (Rs. One Hundred and Sixty Crore only)**	**CARE AA- ; Stable (Double A minus; Outlook: Stable)**	**Reaffirmed**

Details of instruments/facilities in Annexure-1

Detailed Rationale and Key Rating Drivers

The rating assigned to Bandhan Bank Ltd (BBL) continues to draw strength from the experienced promoter, diversification of loan portfolio after merger of Gruh Finance Ltd (GFL), increasing operational presence, mobilization of substantial deposits base with high proportion of retail deposits, robust capitalization profile, strong liquidity profile, comfortable asset quality with seasoned portfolio, healthy return indicators and legacy of established credit operations in micro-finance with strong operational network in the non-urban areas.

The rating is, however, constrained by the dominance of micro-advances in the lending portfolio and geographical concentration of operations, though reduced post amalgamation of GFL. Micro-advances remained high at about 64% of advances as on March 31, 2020 exposing the bank to the inherent risks in the micro finance industry including unsecured lending, event based risks, socio-political intervention and operational risks related to cash based transaction along with marginal profile of borrowers. The bank continues to have geographical concentration in eastern and north eastern India at about 60% of its branch presence.

Furthermore, the rating takes note of housing finance being a relatively new area of business for BBL and foray into newer area of general banking business which is characterized by intense competition. The stake of the non-operative financial holding company (NOFHC) has reduced to 60.96% from 82.26% after the amalgamation of GFL. However, it continues to remain higher than the stipulated 40%. Complying with RBI stipulation to reduce promoter’s stake as per the licensing norms and any development in this regard is a key rating monitorable.

The rating also takes note of the operational challenges being faced on account of the outbreak of Covid-19 and expected pressure on asset quality for which the bank has already created significant amount of provisions. The ability to grow the loan book and deposits and control credit costs considering the uncertainty with respect to achieving normalcy remains to be seen. The bank has extended moratorium to its borrowers as per the RBI guidelines, however, the ability of the borrowers to pay back immediately after the moratorium is over remains critical.

Rating Sensitivities

Positive factors *- Factors that could lead to positive rating action/upgrade*

- Reduction in concentration of micro finance loan book below 30% on a sustained basis.
- Further improvement in geographical diversification
- GNPA below 0.5% on a sustained basis

Negative Factors *- Factors that could lead to negative rating action/downgrade*

- Significant weakening of asset quality on a sustained basis
- Deterioration in capital ratios with the Tier I capital ratio below 15%
- Any regulatory action on inability to reduce promoter holding impacting operations

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoter

BBL was promoted by BFSL and is its step down subsidiary. BFSL holds 60.95% stake in BBL presently through a Non-Operative Financial Holding Company (NOFHC) named Bandhan Financial Holdings Ltd (BFHL).

BFSL was promoted by Mr. Chandra Shekhar Ghosh (MD & CEO of BBL) who has an aggregate experience of over two decades in micro-financing activity which forms the major part of business for the bank. Moreover, the shareholders of BBL comprises of reputed investors like HDFC Limited (post-merger of GFL), Nomura India Investment Fund and GIC through its group company Caladium Investment PTE Limited.

Increasing operational presence

BBL commenced its operations on August 23, 2015 with a network of around 501 branches across India. The operational presence has been increasing over the years and the branch network further increased from 986 as on March 31, 2019 to 1018 as on March 31, 2020. The operations of BBL are also supported by around 3541 Door step services (DSCs) including

Gruh centres, which facilitate the microfinance operations of BBL. Including the branches, DSCs and Gruh centres, BBL had 4559 banking outlets as on March 31, 2020.
Presently the bank has presence in 34 out of 36 states and union territories in India.

Substantial deposit base with increasing retail deposits
The total deposit base of BBL increased from Rs.43,232 crore as on March 31, 2019 to Rs.57,082 crore as on March 31, 2020 with significant increase in term deposits (increased from Rs.25,614 crore as on March 31, 2019 to Rs.36,054 crore as on March 31, 2020).
The proportion of savings and demand deposit is around 36.84% as on March 31, 2020. Although, microfinance borrowers are a large part of total customer base, they contributed only 5.75% to total deposits indicating the ability of the bank to garner deposits from a newer customer base. Furthermore, the retail deposits constituted 78.4% of total deposits showing a more granular deposit profile.

Robust capitalization
IPO of BBL in March 2018 had led to significant improvement in the net worth of the bank as on March 31, 2018. With issue of shares to shareholders of GFL and accretion of profits to reserve, net worth further increased significantly to Rs.15,195 crore as on March 31, 2020.
Overall CAR and Tier I CAR of the bank remained healthy at 27.43% and 25.19% as on March 31, 2020, respectively and significantly above the regulatory requirement. The CAR as at March 31, 2020 has moderated as compared to CAR as at March 31, 2019 despite increase in tangible net worth mainly due to higher leverage of GFL. The overall gearing increased to 4.83x as on March 31, 2020 as against 3.91x as on March 31, 2019 due to inclusion of debt funded portfolio of GFL.
Healthy capitalization provides significant headroom for the bank to pursue growth in a highly competitive industry.

Portfolio and product diversification driven by inclusion of GFL's portfolio in FY20
BBL's portfolio predominantly consisted of micro loans with 86% of the loans as micro-loan as on March 31, 2018 as well as March 31, 2019.
The proportion of micro loans reduced significantly to 64% as on March 31, 2020, mainly due the inclusion of housing loan portfolio of GFL. GFL's portfolio constituted 25% of BBL's AUM as on March 31, 2020. The proportion of micro loan is expected to moderate in the medium term with higher penetration of general banking business of BBL and inclusion of expansion of GFL portfolio. Risk related to lack of expertise in such newer product (mortgage loan) and geography (Central and Western India) is expected to be mitigated to some extent with the induction of GFL's task force.
As on March 31, 2020, BBL's Priority sector assets as a percentage of advances were 91% (including GFL portfolio) as against RBI's norm of 40%.

Comfortable asset quality with seasoned portfolio
The asset quality of BBL improved with GNPA decreasing from 2.04% as on March 31, 2019 to 1.48% as on March 31, 2020 mainly due to the merger as the total loan assets increased substantially compared to the GNPAs. The asset quality is expected to remain under pressure going forward due to the impact of COVID 19. However, the bank has provided around Rs.690 crore for potential COVID 19 impact in Q4FY20 and had earlier provided for additional Rs.200 crore in Q3FY20 for the portfolio in Assam which was witnessing stress due to various socio-political issues.
As on March 31, 2020, around 52% of the loan was for borrowers in micro-finance with 4th cycle and above, which is an indication of seasoned portfolio with matured borrowers.

Healthy return indicators though dip in Q4FY20 on account of additional provisions
Total income of BBL increased substantially by about 61% in FY20 over FY19 with significant growth in interest income and other income driven by the growth in AUM.
NIM witnessed marginal moderation at 8.54% in FY20 from 8.93% in FY19 with increase in yield on advances negated by higher cost of borrowings. Average cost of borrowing was higher with the merger of GFL (which had higher cost borrowings) and decrease in the proportion of CASA deposits in deposits mix.
The operating expenses (opex)/Average total assets decreased marginally from 3.59% in FY19 to 3.28% in FY20 mainly due to merger (lower opex of GFL). The credit cost increased from 1.46% in FY19 to 1.88% in FY20, mainly due to the provision created on account of COVID 19 and write-offs made during the year. ROTA, however, increased from 3.87% in FY19 to 4.08% in FY20.
The bank reported PAT of Rs.3,024 crore in FY20 post-merger of GFL as against standalone PAT of Rs.1,952 crore in FY19.

Key Rating Weaknesses
Concentration of micro-advances in portfolio and geographical concentration
The proportion of micro loans reduced to 64% as on March 31, 2020, post the inclusion of housing loan portfolio of GFL. However, the same continues to remain high exposing BBL to risks inherent in the micro-finance business including event risk, unsecured nature of lending, marginal profile of borrowers, socio-political risk and risk related to cash-based

transactions. Further reduction in micro loan portfolio with higher penetration of general banking business of BBL and successful expansion of housing finance portfolio is a key rating sensitivity.

Though the micro-finance portfolio has shown higher resilience in the past in times of crisis, the performance in the current uncertain situation on account of the outbreak of Covid-19 remains to be seen. The bank had offered moratorium to a large number of its customers as per RBI's guidelines on Covid-19 Regulatory Package. Consequently, there might be challenges if a higher proportion of total customers continue to opt for moratorium.

The inheritance of the micro-advance portfolio by BBL from BFSL is primarily concentrated in West Bengal, which has resulted in inherently higher concentration of portfolio in the state. The top three states (West Bengal, Gujarat and Assam) contributed to about 71% of the portfolio as on March 31, 2020.

As a result of the amalgamation, the concentration of branches in the east has reduced from 51% as at March 31, 2019 to 47% as at March 31, 2020, whereas the concentration of branches in Central India has increased from 16% as at March 31, 2019 to 18% as at March 31, 2020. However, the concentration continues to remain high.

Intense competitive pressure

Despite inheritance of established micro finance business of BFSL which occupied the leadership position in the MFI sector, the operations of BBL is expected to face intense competition in the light of RBI granting new banking licenses comprising of payment banks and small finance banks for deepening financial inclusion objectives of the regulator. Further, in the retail lending sector, BBL has to establish its track record and appeal to newer urban customers amidst intense competition from established public sector and private sector banks which already has a major share of the market. BBL's ability to gain from merger of GFL also remains to be seen.

Regulatory Risk

The bank was required to reduce promoters holding (NOFHC) to 40% within three years of operation i.e. by August, 2018 as per RBI's new banking licensing guidelines. Due to non-compliance with the same, RBI had earlier imposed restrictions on opening of branches by the bank and a penalty was also imposed. The amalgamation has led to reduction in promoter holding to 60.95%. However it is still above the 40% requirement. Developments in regard to stake dilution are a key monitorable.

Liquidity: Strong

The structural liquidity statement of BBL indicates positive cumulative mismatches across all time buckets. The liquidity profile of the bank is strong and supported by the high capitalization levels apart from maintaining the regulatory CRR and SLR levels. Further, the lower tenure of advances financed (majority of micro loan has a tenure of 12-24 months) vis-à-vis the longer tenure of funding profile also provides liquidity comfort.

Access to IBPC market is also likely to support the liquidity profile of the bank, since a large part of the portfolio of BBL (around 91% of gross advances as on March 31, 2020), qualifies for priority sector lending requirements. Excess SLR investments as on March 31, 2020 were Rs. 5907 crore and Liquidity Coverage Ratio was around 129%. The deposits base has also witnessed growth up to April 2020.

Analytical Approach: Standalone

Applicable Criteria

[Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings]
[CARE's Policy on Default Recognition]
[Financial ratios –Financial Sector]
[Bank – CARE's Rating Methodology for Banks]

About the Company

BBL was incorporated on Dec.23, 2014, promoted by BFSL as its step down subsidiary. BFSL was a NBFC-MFI which was engaged in the business of lending to individual women borrowers under 'Group based individual lending' model and operated across 22 states & Union Territories of India. BFSL was granted approval by Reserve Bank of India (RBI) on April 2, 2014 to set up a bank under 'Guidelines on Licensing of New Banks in the Private Sector'. Subsequently, on June 17, 2015, RBI granted the license to BBL to carry out the banking business in India. BBL formally commenced its banking operations on Aug.23, 2015 with 501 branches on a pan India basis. In line with the terms of Business Transfer Agreement (BTA) dated Feb.11, 2015 entered between BFSL and BBL, the entire assets/liabilities of BFSL were transferred to BBL.

BBL was listed in March 2018 through an IPO and Rs. 3662 crore was infused in the bank.

The merger of GFL with the bank was completed in October 2019 after receipt of all required regulatory approvals with effective date of October 17, 2019 and appointed date of January 1, 2019. GFL was a Housing Finance Company with gross loan portfolio of Rs.17,288 crore as on March 31, 2019 concentrated mainly in West and Central India with HDFC Limited

being the single largest shareholder (57.86%). GFL operated primarily in the rural and semi urban areas of Gujarat and Maharashtra.
As on March 31, 2020, the combined AUM of GFL and BBL was Rs.71,845 crore (Rs.44,776 crore as on March 31, 2019 BBL standalone) spread across 34 states & Union Territories through 4559 branches (includes branches, DSCs & GFL centres).

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Total income	7,707.10	12,434.68
PAT	1,951.50	3,023.73
Interest coverage (times) (after provision)	2.78	2.19
Total Assets	56,441.70	91,717.79
Net NPA (%)	0.58	0.58
ROTA (%)	3.87	4.08

A: Audited
CARE has made analytical adjustments while calculating the ratios.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History (Last three years): Please refer Annexure 2

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
Debt-Subordinate Debt	INE545U08019	September 02, 2014	14.536	September 02, 2021	160.00	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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Term Loan	LT	-	-	-	-	-	1)Withdrawn (06-Oct-17)
2.	Debt-Subordinate Debt	LT	160.00	CARE AA-; Stable	-	1)CARE AA-; Stable (06-Jan-20)	1)CARE AA- (Under Credit watch with Developing Implications) (08-Jan-19) 2)CARE AA-; Stable (10-Oct-18)	1)CARE AA-; Stable (06-Oct-17)

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

Contact us

Media Contact
Name: Mradul Mishra
Contact no: +91-22-6837 4424
Email ID: mradul.mishra@careratings.com

Analyst Contact
Name: Ms. Mamta Muklania
Contact no. : 033-4018 1651/98304 07120
Email ID: mamta.khemka@careratings.com

Relationship Contact
Name: Mr. Lalit Sikaria
Contact no. : 033-40181607
Email ID: lalit.sikaria@careratings.com

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.

****For detailed Rationale Report and subscription information, please contact us at www.careratings.com**