Canara Bank

March 03, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating1	Rating Action
Proposed-Basel III Tier II bonds	3000 Rs. Three thousand crore only	CARE AAA (Triple A) (Credit watch with developing implications)	Assigned; Placed on credit watch with developing implications

Details of instruments/facilities in Annexure-1

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's 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 has rated the Tier-II bonds under Basel III after factoring in the additional feature of PONV.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bond issue of Canara Bank (CB) derives strength from majority ownership by Govt. of India (GoI) from which it has been receiving timely capital infusion, experienced management and governance, established retail franchise with strong network in southern states of India, comfortable capitalization levels with total CAR well above regulatory requirements post equity infusion during H1FY20, moderate resource profile with relatively low CASA share but high retail deposit and comfortable liquidity profile. These rating strengths are partially offset by moderate asset quality of the Bank with high NNPA resulting in relatively higher NNPA to Networth compared to its peers though improving, continued slippages resulting in higher provisioning impacting profitability of the bank and modest provision coverage (including technical write-offs). Bank's profitability parameters have witnessed improvement during 9MF20 with improvement in recoveries.

The rating is placed under watch with developing implications on account of ongoing amalgamation process of Syndicate Bank into Canara Bank following directive from Ministry of Finance, GOI. The amalgamated bank is likely to be the 4th largest PSB post amalgamation. CARE will continue to monitor the development including challenges in successful integration and take appropriate rating call once clarity emerges on the merged entity's financial and business risk profile.

<u>Rating Sensitivities</u>

Negative Factors

- Significant slippages impacting earnings profile and deterioration in Net NPA to networth.
- Deterioration in capitalisation levels on a sustained basis.

Detailed description of the key rating drivers

Key Rating Strengths

Majority ownership by Government of India (GOI) and demonstrated support: Government of India (GoI) continues to have majority stake in the bank. GOI has demonstrated support by way of capital infusion in the bank. As part of its recapitalization plan, GOI had infused Rs.7,627 crore in CB during FY14-FY18 but no equity infusion in FY19. Further, GOI had infused Rs.6,571 crore during September 2019, consequently, the shareholding of GoI increased from 70.62% as on March 31, 2019 to 78.52% as on December 31, 2019.

During Aug'19, Ministry of Finance, GOI, proposed to amalgamate Syndicate Bank with Canara Bank w.e.f April 01, 2020. Merger process is on track with approval in place from respective Boards of the bank, however ability of the Banks to successfully integrate the operations and attain synergy remains to be seen. The amalgamated Bank is likely to be the 4th largest PSB post amalgamation increasing the strategic importance of the bank.

Comfortable capitalization levels: Bank's CAR and Tier-I CAR stood modest at 11.90% and 9.04% respectively as on March 31, 2019. However aided by profitability during 9MFY20 coupled with equity infusion of Rs.6571 crore from GOI bank's CAR and Tier-I CAR levels improved to 13.86% and 11.05% respectively as on Dec'19 and remain comfortably above the regulatory requirements of 11.50% and 9.50% respectively as on March 31, 2020. Focus on lending to better rated clients, sectors has

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

resulted in lower capital requirement for Bank. RWA as a % of gross advances has improved from 87.74% as on March 31, 2018 to 79.34% as on March 31, 2019 and was at 81.87% as on Dec’19.

Established franchise and deposits base with a strong presence in the southern states: Total business of the bank stood at Rs.10.63 lakh crore as on December 31, 2019 with deposit base of Rs.6.25 lakh crore and advances of 4.38 lakh crore. Bank has an established presence with network of 6328 branches and 8,873 ATMs as on December 31, 2019 especially in Karnataka with close to 1000 branches. Bank has a strong deposit base especially in Karnataka. Going forward, with the merger of Syndicate Bank with Canara Bank, the amalgamated Bank is expected to have a dominant presence in southern states of India.

Moderate resource profile with relatively low CASA share but high retail deposit: Bank has a moderate resource profile with low CASA share of 30.93% of domestic deposits as on December 31, 2019. However, it has a strong retail deposit base which forms about 40% of the total deposits as on December 31, 2019. Bulk deposits formed 25.01% of the total deposits as on March 31, 2019 and the same has remained stable at 25.08% as on December 31, 2019.

Key Rating Weaknesses

Moderate profitability although marginal improvement in 9MFY20: Despite decrease in non-interest income on account of lower treasury profits, bank reported growth in total income of 10.77% aided by healthy growth in interest income in line with growth in advances. Net interest income of the bank has witnessed growth of 19.03% aided by improvement in yield on advances and cost of deposits remaining stable during FY19. Further with lower provisioning in FY19, the Bank reported net profit of Rs.347 crore in FY19 as against net loss of Rs.4,222 crore in FY18. Bank’s ROTA was low at 0.05% in FY19 as against negative 0.71% in FY18.

Bank’s profitability has witnessed further improvement during 9MFY20 and reported PAT of Rs.1024 crore aided by lower provisions and healthy growth in non-interest income. In general, Bank’s profitability has been under pressure due to relatively high cost to income ratio and high provisions. Bank’s provision coverage ratio (including technical write offs) was modest at 70.79% as on December 31, 2019 improving from 68.13% as on March 31, 2019 and compares with PSU average of around 76%. However, excluding technical write offs provision coverage ratio of Bank continues to remain low at 41.48% as on Mar’19 (Mar’18: 39.87%) and the same stood at 41.77% as on December 31, 2019 leading to higher provisioning requirement due to ageing of NPA.

Moderate asset quality with high NNPA and continued slippages albeit improvement during FY19 and 9MFY20: Bank’s asset quality continues to remain moderate albeit improvement during FY19 and 9MFY20. Bank’s Gross NPA ratio improved to 8.83% (March 31, 2018: 11.85%) and Net NPA ratio improved to 5.37% (March 31, 2018: 7.48%) aided by lower net slippages, higher amount of recoveries and write-off during FY19. Bank’s asset quality has further improved with GNPA and NNPA at 8.36% and 5.05% respectively as on December 31, 2019 aided by recoveries of Rs.7,109 crore and write-offs of Rs.5412 crore. Bank received equity infusion of Rs.6,751 crore from GOI which resulted in improvement of NNPA/ Net worth to 61.52% as on December 31, 2019 as against 86.97% as on March 31, 2019 however the same continues to be higher compared to its peers. Further, deterioration of the same on account of continued slippages will be a key rating monitorable. Going forward, slippages are expected to remain modest given the relatively low exposure to watchlist accounts. This along with recoveries is expected to help reduce the net NPA levels of the bank.

Liquidity: Strong

According to the Bank’s structural liquidity statement (SLS) as on December 31, 2019, there are no negative cumulative mismatches in up to 1 year maturity bucket. Further, bank has maintained an excess SLR investment of Rs.46,339 crore as on December 31, 2019. These factors provide cushion to the bank’s liquidity profile. CB’s liquidity coverage ratio remained adequate at 128.58% against the minimum regulatory requirement of 100%.

Analytical approach: Standalone along with expected support from GOI.

Applicable Criteria

Criteria on assigning ‘outlook’ and ‘credit watch’

CARE’s Policy on Default Recognition

Financial Ratios – Financial Sector

Rating Methodology – Banks

About the Company

Canara Bank (CB) is a Bengaluru-based public sector bank which was established in 1906. Government of India is the majority shareholder holding 78.52% stake in the Bank followed by LIC of India holding 6.74% as on December 31, 2019. As on

December 31, 2019, the Bank had 6328 branches, of which 1825 are in rural, 2007 in semi urban, 1224 in urban and 1272 in metro areas. The Bank also has 5 overseas branches located at Johannesburg, New York, London, Hong Kong and Dubai. The Bank has 8 subsidiaries, 3 associate and 1 Joint Venture companies. Mr. Lingam Venkata Prabhakar is the MD and CEO, w.e.f February 01, 2020, who is assisted by a team of Executive Directors and General Managers heading various departments. As part of recapitalization plan, GOI has infused Rs.6,571 crore of equity capital during September 2019. As on December 31, 2019, the Bank had advances of Rs. 4,38,210 crore and deposits of Rs.6,25,240 crore.

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

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	48195	53385
PAT	-4222	347
Interest coverage (times)	1.33	1.33
Total Assets	604590	684983
Net NPA (%)	7.48	5.37
ROTA (%)	-0.71	0.05

A: Audited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Proposed-Bonds-Tier II Bonds	-	Proposed	Proposed	3000.00	CARE AAA (Under Credit watch with Developing Implications)

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Proposed-Bonds-Tier II Bonds	LT	3000.00	CARE AAA (Under Credit watch with Developing Implications)	-	-	-	-

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Not Applicable. Proposed instrument.

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

Analyst Contact
Group Head Name - Himanshu Jain
Group Head Contact no.- 080-46625528
Group Head Email ID- himanshu.jain@careratings.com

Relationship Contact
Name: V Pradeep Kumar
Contact no.: 044-28497812/0811
Email ID : pradeep.kumar@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**