JULY 29, 2016

CARE REAFFIRMS THE RATING ASSIGNED TO THE BASEL III COMPLIANT ADDITIONAL TIER I PERPETUAL BOND ISSUES OF INDIAN OVERSEAS BANK

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Remarks
Basel III Compliant Additional Tier I Perpetual Bonds @	1,000 (Rupees One thousand crore only)	CARE BBB [Triple B]	Reaffirmed
Basel III Compliant Additional Tier I Perpetual Bonds (Proposed Public Issue) @	1,000 (Rupees One thousand crore only)	CARE BBB [Triple B]	Reaffirmed

@ CARE has rated the aforesaid Basel III Compliant Additional Tier-I (AT1) Perpetual Bonds after taking into consideration its key features as 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, coupon payment may be paid subject to availability of sufficient revenue reserves and/or credit balance in profit and loss account provided the bank meets the minimum regulatory requirements for Common Equity Tier I [CET I], Tier I and Total Capital Ratios at all times and subject to the requirements of 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 March 31, 2019, or written-off / converted into common equity shares on occurrence of 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's definition of default and as such these instruments may exhibit a somewhat sharper migration of the rating compared with the conventional subordinated debt instruments.

Rating Rationale

The rating assigned to the Basel III Compliant AT1 Perpetual bond issues of Indian Overseas Bank (IOB) continues to derive strength from the majority ownership by Government of India (GoI), long standing track record of operations and strong presence of the bank in South India. The rating also factors in the proposed equity infusion of Rs.3,101 crore recently announced by GoI. The rating takes note of the bank's performance in FY16 (refers to the period April 1 to March 31) characterised by losses and deterioration in asset quality due to significant increase in provisions for non-performing assets (NPA) subsequent to Asset Quality Review (AQR) of RBI. In view of significant NPA additions during FY16, profitability of the bank is likely to be influenced by extent of provisioning in the near term.

Given the features of the AT1 bonds, going forward, ability of the bank to earn adequate profits after provisioning is vital. Though the revenue reserve was positive, accumulated losses stood relatively higher as on March 31, 2016 and CARE would continue to monitor the position of the same. Going forward ability of the bank to mobilise capital in periodical manner to meet the increasing capital adequacy levels as per regulatory requirements and improve its profitability amidst higher provisioning requirement are key rating sensitivities.

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

Background

Indian Overseas Bank (IOB) established in 1937 at Chennai, is one of the larger public sector banks with a sizeable footprint in South India. As on March 31, 2016, the bank had a network of 3,397 domestic branches (1036 rural, 960 semi-urban, 748 urban and 653 metropolitan branches), 8 overseas branches, 3 representative office and an ATM network of 3973, spread across the country. As on June 30, 2016, GoI held 73.58% stake in IOB.

During FY16, IOB reported a net loss of Rs.2,897 crore on a total income of Rs.26,046 crore. Gross NPA and Net NPA stood at 17.40% and 11.89% respectively as on March 31, 2016.

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

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.

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