Union Bank of India

January 07, 2020

Ratings

Instrument	Amount (Rs. Crore)	Rating[1]	Rating Action
Lower Tier II Bonds (Basel II)	800.00 (Rupees Eight Hundred crore only)	CARE AA+ (Double A Plus) (Credit watch with developing implications)	Continues to be on credit watch
Upper Tier II Bonds (Basel II) @	1,000.00 (Rupees One Thousand crore only)	CARE AA (Double A) (Credit watch with developing implications)	Continues to be on credit watch
Perpetual Bonds (Basel III) #	2,000.00 (Rupees Two Thousand crore only)	CARE AA- (Double A Minus) (Credit watch with developing implications)	Continues to be on credit watch
Total	**3,800.00 (Rupees Three Thousand and Eight Hundred crore only)**		

Details of instruments/facilities in Annexure-1

@: CARE has rated the aforesaid Upper Tier II Bonds one notch lower than the Lower Tier II Bonds in view of their increased sensitiveness to the Union Bank of India's Capital Adequacy Ratio (CAR), capital raising ability and profitability during the long tenure of the instruments. The rating factors in the additional risk arising due to the existence of the lock in clause in hybrid instruments. Any delay in payment of interest/principal (as the case may be) following the invocation of the lock-in-clause, 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 rating compared to conventional subordinated debt instruments.

#: CARE 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 including statutory reserves and/or credit balance in profit and loss account and excluding share premium, revaluation reserve, foreign currency translation reserve, investment reserve and reserves created on amalgamation provided the bank meets the minimum regulatory 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 March 31, 2019, 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's 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 the debt instruments of Union Bank of India continue to be under watch with developing implications following the development involving communication from Ministry of Finance, GOI on amalgamation of Union Bank of India (UBI) with Andhra Bank and Corporation Bank wherein UBI would be the anchor bank. The amalgamated bank is likely to be the 5th largest public sector bank in terms of business post amalgamation. Given the number of approvals required and timelines to obtain the same and challenges to be encountered in successfully integrating the operations, CARE has placed the ratings under watch with developing implications. CARE will continue to monitor the development and take appropriate rating call once clarity emerges on the merged entity.

The ratings assigned to various debt instruments of Union Bank of India (UBI) take into consideration majority ownership by Government of India (GoI) and its demonstrated capital support as well as support in terms of management and governance.

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

The rating also takes into consideration the long standing track record of operations and established franchise with an extensive branch network, improved capitalization levels, comfortable liquidity profile, strong resource profile, and moderate advances profile.
The ratings remain constrained on account of the bank's moderate profitability and asset quality parameters.
Continued ownership and support from GOI, asset quality, profitability and capital adequacy are key rating sensitivities.

Rating Sensitivities
Positive Factors

- Continued majority shareholding and support by GOI
- Improvement in asset quality parameters on a sustained basis
- Improvement in profitability on a sustained basis

Negative Factors

- Deterioration in asset quality parameters on a sustained basis
- Deterioration in capitalisation levels
- Deterioration in profitability on a sustained basis

Detailed description of the key rating drivers
Key Rating Strengths
Majority ownership by GoI, continued capital support and support in terms of management and governance
The bank's credit profile derives considerable comfort and expectations of capital support in the times of stress from parentage of Government of India (GOI) being the majority shareholder in Union Bank of India holding 74.27% stake as on September 30, 2019. The rating further derives comfort from demonstrated capital support by GOI in the form of regular equity infusion over the past few years. During FY19 (refers to period from April 01 to March 31), GOI infused Rs.4,112 crore of equity capital (Rs.4,524 during FY18) as a part of government's Rs.2.11 lakh crore Recapitalization programme for public sector banks (PSBs).
Further, during the quarter ended September 30, 2019, the bank received Rs.11,768 crore of equity capital from GOI towards preferential allotment of equity shares. GOI is expected to continue its majority shareholding and provide capital support in times of stress to the bank and is a key rating sensitivity.

Long standing track record and established franchise
The bank has a long standing track record of nearly 100 years and has an established national franchise through a pan-India network of 4,285 branches (4,282 domestic branches) and 6,798 ATMs excluding 5,586 Micro – ATMs. About 59% of the branches are located in the rural and semi-urban markets, followed by urban and metro areas at an equal share of 20%, as on September 30, 2019. Uttar Pradesh is the state with highest number of branches (934) followed by Maharashtra and Madhya Pradesh with 505 and 288 branches respectively. The bank has overseas branches in Hong Kong, Sydney and Dubai, in addition to representative office in Abu Dhabi. Operations in UK are through its wholly owned subsidiary, Union Bank of India (UK) Ltd.

Improved capitalization levels
During FY19, UBI raised equity capital of Rs.4,680.32 crore (Rs.4,112 crore infused by GOI and Rs.568.32 crore through ESPP). The capital raising helped the bank to report Capital Adequacy Ratio (CAR) of 11.50% (P.Y.: 11.79%) [Tier I CAR: 9.07% (P.Y.: 9.02%)] and Common Equity Tier I (CET I) Ratio of 7.60% (P.Y.: 7.71%) as on March 31, 2018. Further, the bank called off Basel II compliant Additional Tier I Bonds of Rs.340 crore and redeemed Tier II Bonds of Rs.1,200 crore on maturity.
During the quarter ended September 30, 2019, the Bank received Rs.11,768 crore from Government of India towards preferential allotment of equity shares, which has been considered as a part of CET1 capital, pending allotment of equity shares. CAR under Basel III improved to 15.14% as on September 30, 2019 as compared to minimum regulatory requirement of 11.50%, whereas the Tier I CAR as of September 30, 2019 stood at 12.83%. The CET1 ratio was 11.46% as against regulatory minimum of 8.00%.
Earlier during FY18, UBI raised equity capital of Rs.6,524 crore (Rs.4,524 crore infused by GOI and Rs.2,000 crore through QIP), which helped the bank to report CAR of 11.50% [Tier I CAR: 9.07% and CET-1 Ratio of 7.60%, as on March 31, 2018.

Comfortable liquidity profile and stable resources profile
The liquidity position of the bank was comfortable with well-matched ALM profile as on September 30, 2019 with positive cumulative mismatches in all time buckets up to 6 months and the mismatches are well within the RBI / Board defined tolerance limits. The bank had excess SLR investments of Rs.37,450 crore as on September 30, 2019. The bank's Liquidity Coverage Ratio (LCR) stood at 186.21% as on September 30, 2019 (March 31, 2019: 156.87%) and its High Quality Liquid Assets (HQLA) stood at Rs.1,19,465.21 crore as on September 30, 2019 (Rs.89,363 crore as on March 31, 2019). Minimum

requirement of LCR as stipulated by RBI is 100% by January 01, 2019. Further, the bank's healthy deposit rollover rate of 70-75% and capital raising ability provide comfort. The bank reported a deposit base of Rs.4,15,915 crore as on March 31, 2019 as compared to Rs.4,08,502 crore as on March 31, 2018 with CASA proportion of 34.70% as on March 31, 2019 as compared to 34.10% as on March 31, 2018. The deposits as on September 30, 2019 stood at Rs.4,42,879 crore with CASA proportion of 33.80%.

Moderate advances profile

During FY19, the bank saw credit growth at 2.83% with Net Advances of Rs.296,932 crore as on March 31, 2019 as against Rs.288,761 crore as on March 31, 2018. Domestic advances grew by 7.84% to Rs.3,10,932 crore as on March 31, 2019 vis-à-vis Rs.2,88,336 crore as on March 31, 2018. The RAM (Retail, Agriculture and MSME) sector stood at Rs.1,73,237 crore as on March 31, 2019 as against Rs.1,58,642 crore as on March 31, 2018, growing by 9.2%.

Key Rating Weaknesses

Average profitability parameters

During year ended March 31, 2019, the bank reported a net loss of Rs.2,947.45 crore as against loss of Rs.5,247.37 crore for the year ended March 31, 2018. The major driver for reduction in net loss is the decline of 20% in provisions and contingencies, with stable levels of total income and total expenditure. The bank's cost to income ratio for FY19 was at 48.80% (P.Y.: 47.26%), Net Interest Margin (NIM) of 2.11% (P.Y.: 2.10%) and Return on Total Assets (ROTA) of -0.61% (P.Y.: -1.18%).

For the half-year ended September 30, 2019, the bank reported net loss of Rs.969 crore on total income of Rs.20,444 crore as against profit of Rs.269 crore on total income of Rs.19,347 crore during the immediately preceding half-year. The bank has cost to income ratio of 45.39%, Net Interest Margin (NIM) of 2.14% and Return on Total Assets (ROTA) of -0.38%. Operating profit stood at Rs.2,240 crore for the quarter ended September 30, 2019 as against Rs.1,886 crore for the immediately preceding quarter. The same stood at Rs.1,832 crore for the quarter ended September 30, 2018.

Moderate asset quality parameters

As on March 31, 2019, the bank reported Gross NPA (GNPA) ratio, Net NPA (NNPA) ratio and Net NPA to Net-worth (NNPA/NW) ratio of 14.98% (P.Y.: 15.73%), 6.85% (P.Y.: 8.42%) and 106.73% (P.Y.: 131.27%) respectively. The bank reported gross stressed assets (GNPA + Standard Restructured Assets as % of Gross Advances) and net stressed assets (NNPA + Standard Restructured Assets as % of Net Advances) of 15.4% (P.Y.: 16.12%) and 6.7% (P.Y.: 8.14%) respectively. The bank made a cash recovery of Rs.4,509 crore in addition to upgradation of accounts to the tune of Rs.1,938 crore. Provision coverage ratio has risen by 908 bps to 66.2% as on March 31, 2019 as against 57.2% as on March 31, 2018. As on September 30, 2019, the bank reported GNPA, NNPA and NNPA/NW of 15.24%, 6.98% and 66.58% respectively (P.Y.:15.74%, 8.42% and 131.15% respectively). The bank reported gross stressed assets and net stressed assets of 15.7% and 6.9% respectively.

On November 20, 2019, the bank disclosed on stock exchanges that there was a divergence for reporting and provisioning of NPA for FY19 ascertained by RBI at Rs.1,588 crore, post SEBI's directive to all listed banks to disclose any divergence in bad loan provisioning. SEBI noted that disclosures in respect of divergence and provisioning are in the nature of material events and hence necessitate immediate disclosure. Considering the divergent provisioning, its adjusted (notional) loss would be Rs.3,978 crore for FY19 from Rs.2,947 crore earlier. The bank had already made provisions of approximately Rs.400 crore in the earlier quarters, and the incremental impact of additional provisioning was to the tune of Rs.1,100 crore in Q2FY19.

Liquidity Profile: Strong

The asset liability maturity (ALM) profile as on September 30, 2019 had cumulative mismatches in the time buckets beginning from 6 months, however the mismatches are well within the RBI / Board defined tolerance limits. The bank had excess SLR investments of Rs.37,450 crore as on September 30, 2019, which provided the bank adequate liquidity. In addition, the bank has access to borrowing from RBI's Liquidity Adjustment Facility (LAF) and Marginal Standing Facility (MSF) along with cash reserves with RBI which provide comfort in meeting any liquidity pressures. The bank's Liquidity Coverage Ratio (LCR) stood at 186.21% as on September 30, 2019 (March 31, 2019: 156.87%) and its High Quality Liquid Assets (HQLA) stood at Rs.1,19,465 crore as on September 30, 2019 (Rs.89,363 crore as on March 31, 2019).

Analytical approach: The ratings are based on standalone profile of the bank (merged entity) and continue to factor in strong support from Government of India (GOI) which holds majority shareholding in the bank.

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE Policy on Default Recognition

CARE's Rating Methodology For Banks
Bank - Rating framework for Basel III instruments (Tier I & Tier II)
Financial ratios - Financial Sector
Rating Methodology: Factoring Linkages in Ratings

About the Company
Union Bank of India (UBI) was established in 1919. The bank has total asset base of 5,26,058 crore as on September 30, 2019 (Rs. 4,86,602 crore as on March 31, 2019). Post the proposed amalgamation with Andhra Bank and Corporation Bank, UBI shall become the fifth largest PSB with an estimated business of Rs.14.59 lakh crore, from the current level of Rs.7.70 crore as on September 30, 2019. Government of India (GOI) holds 74.27% shareholding in UBI as on September 30, 2019. The bank has a pan India network of 4,285 branches (4,282 domestic branches) and 6,798 ATMs excluding 5,586 Micro – ATMs as of September 30, 2019. The bank has a pan India network of 4,285 branches (4,282 domestic branches) and 6,798 ATMs excluding 5,586 Micro – ATMs as of September 30, 2019. Union Bank of India is headed by Mr. Rajkiran Rai who took over as Managing Director & Chief Executive Officer (MD & CEO) of the bank w.e.f. July 01, 2017. The bank has overseas branches in Hong Kong, Sydney and Dubai, in addition to representative office in Abu Dhabi. The Bank operates in UK through its wholly owned subsidiary, Union Bank of India (UK) Ltd. The Bank has 27 extension counters, 59 satellite offices and 48 service branches in addition to its regular bank branches as of September 30, 2019.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	37,738	38,541
PAT	(5,247)	(2,947)
Total Assets	480,841	4,86,602
Net NPA (%)	8.42	6.85
ROTA (%)	(1.18)	(0.61)

A: Audited

** Total assets and Networth is net of deferred tax assets and intangible assets. NIM and ROTA have been computed using CARE's calculations*

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 I- Instrument Details

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr)	Rating
Upper Tier II Bonds Series XIV-C	INE692A09225	27-Jan-10	8.55 up to 10 years Step up to 9.05 after 10th year if call option not exercised	15 years 27-Jan-25	500	CARE AA; Credit watch with developing implications
Upper Tier II Bonds Series XV	INE692A09233	28-Jun-10	8.48 up to 10 years Step up to 8.98 after 10th year if call option not exercised	15 years 28-Jun-25	500	CARE AA; Credit watch with developing implications
Lower Tier II Bonds	INE692A09241	28-Dec-12	8.9	28-Dec-22	800	CARE AA+; Credit watch with developing implications
Basel III Compliant Perpetual Bonds (ATI Bonds)	INE692A08029	15-Sep-16	9.5	Perpetual	1,000	CARE AA-; Credit watch with developing implications
Basel III Compliant Perpetual Bonds (ATI Bonds)	INE692A08037	04-Nov-16	9	Perpetual	1,000	CARE AA-; 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.	Bonds-Upper Tier II	LT	500.00	CARE AA (Under Credit watch with Developing Implications)	1)CARE AA (Under Credit watch with Developing Implications) (11-Sep-19)	1)CARE AA; Stable (02-Jan-19)	1)CARE AA; Stable (09-Oct-17)	1)CARE AA+; Negative (29-Dec-16) 2)CARE AA+ (19-Aug-16)
2.	Bonds-Upper Tier II	LT	500.00	CARE AA (Under Credit watch with Developing Implications)	1)CARE AA (Under Credit watch with Developing Implications) (11-Sep-19)	1)CARE AA; Stable (02-Jan-19)	1)CARE AA; Stable (09-Oct-17)	1)CARE AA+; Negative (29-Dec-16) 2)CARE AA+ (19-Aug-16)
3.	Bonds-Lower Tier II	LT	-	-	-	-	-	1)Withdrawn (19-Aug-16)
4.	Bonds-Lower Tier II	LT	800.00	CARE AA+ (Under Credit watch with Developing Implications)	1)CARE AA+ (Under Credit watch with Developing Implications) (11-Sep-19)	1)CARE AA+; Stable (02-Jan-19)	1)CARE AA+; Stable (09-Oct-17)	1)CARE AAA; Negative (29-Dec-16) 2)CARE AAA (19-Aug-16)
5.	Bonds-Perpetual Bonds	LT	2000.00	CARE AA- (Under Credit watch with Developing Implications)	1)CARE AA- (Under Credit watch with Developing Implications) (11-Sep-19)	1)CARE AA-; Stable (02-Jan-19)	1)CARE AA-; Stable (09-Oct-17)	1)CARE AA; Negative (29-Dec-16) 2)CARE AA (19-Aug-16)

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.*

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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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