Union Bank of India

October 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+ ; Negative (Double A Plus; Outlook: Negative)	Removed from 'credit watch with developing implications' and Negative Outlook assigned
Upper Tier II Bonds (Basel II) @	500.00 (Rupees Five Hundred crore only)	CARE AA ; Negative (Double A; Outlook: Negative)	Removed from 'credit watch with developing implications' and Negative Outlook assigned
Perpetual Bonds (Tier I) (Basel III) #	2,000.00 (Rupees Two Thousand crore only)	CARE AA- ; Negative (Double A Minus; Outlook: Negative)	Removed from 'credit watch with developing implications' and Negative Outlook assigned

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.

&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 the Common Equity Tier I capital of the bank should be considered as the most appropriate way to prevent the bank from turning non-viable.

#: 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 various debt instruments of Union Bank of India (UBI) are based on the majority ownership by Government of India (GoI) and GoI's demonstrated capital support. In order to better govern the public sector banks, GoI had announced the amalgamation of relatively smaller and weaker banks with larger banks and the merger was effective from April 01, 2020 with Andhra Bank Limited (ABL) and Corporation Bank Limited (CBL) getting amalgamated into UBI which is the anchor bank. Post the merger, the size of the bank has increased significantly and UBI is the fifth largest bank in India in terms of asset size.

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

The ratings also factor in the long standing track record of operations, position of the bank in the financial sector as one of the large sized banks, its established franchise with an extensive branch network spread across the country, comfortable liquidity profile, strong resource profile and moderate advances profile.
The ratings remain constrained on account of the bank's moderate profitability, moderate capital buffers as compared to peer public sector banks and moderate asset quality parameters. Continued ownership and support from GoI, asset quality, profitability and capital adequacy are key rating sensitivities.

CARE has resolved the 'credit watch with developing implications' as the merger of ABL and CBL with UBI has become effective.

Outlook: Negative
The 'Negative' outlook is on account of the expectation of likely stress on the asset quality and profitability in light of Covid-19.With low core capital buffers post the amalgamation, the bank's capital adequacy position going forward is expected to be constrained.
The outlook may be revised to 'Stable' in case of capital infusion in the bank which would increase the capital buffers and improvement in asset quality. The rating may see a downward revision in case of further decline in core capital buffers or further deterioration in asset quality parameters.

Rating Sensitivities
Positive: Factors that could individually or collectively, lead to positive rating action/upgrade:
- Improvement in asset quality parameters with Gross NPA Ratio less than 5% on sustained basis
- Improvement in profitability with ROTA of above 1% on a sustained basis along with improvement in capitalisation levels

Negative: Factors that could individually or collectively, lead to negative rating action/downgrade:
- Reduction in government support and ownership below 50%
- Deterioration in asset quality parameters: Net NPA ratio of over 8% on a sustained basis
- Sustained deterioration in profitability
- Deterioration in capitalization levels

Impact of Covid-19 on the bank's profitability and asset quality:
In terms with the RBI's 'Covid 19 Regulatory Package' on 'Asset Classification and Provisioning', the bank had extended moratorium on payment of installment and / or interest as applicable, falling due between March 1, 2020 and August 31, 2020.
The bank made a Covid-related provision of Rs.125 crore for the quarter ended March 31, 2020, and a further provision of Rs.343 crore for the quarter ended June 30, 2020. Thus, the aggregate provision stood at Rs.683 crore as on June 30, 2020 which stood in excess of the regulatory provisioning of 10%.
RBI came out with a resolution framework on August 06, 2020, to address borrower stress concerns on account of Covid-19. The circular provides for additional provisioning of 10% of the re-negotiated debt exposure. Going forward, the ability of the bank to limit incremental slippages and maintaining healthy capitalisation levels and profitability would key rating sensitivities.

Detailed description of the key rating drivers
Key Rating Strengths
Majority ownership by GoI and continued capital support
The bank's credit profile derives considerable comfort and demonstrated support from GoI in terms of capital infusion, management and governance. CARE expects GoI support to continue support to UBI in the times of stress on account of its majority shareholding (89.07% as on June 30, 2020) and the position of UBI in the financial sector as one of the largest banks in India. GoI has been providing continuous capital support to public sector banks and infused Rs.4,112 crore of equity capital in UBI as a part of GoI's Rs.2.11 lakh recapitalization programme for public sector banks. Further, GoI is expected to continue its majority shareholding in the bank and continued support is a key rating sensitivity.

Long standing track record and established franchise
The Ministry of Finance (MoF), in consultation with Reserve Bank of India (RBI) on August 30, 2019, announced a set of reforms for public sector banks (PSBs), including consolidation, capital infusion and measures to improve governance standards. As part of consolidation, MoF decided amalgamation of 6 PSBs into 4 anchor PSBs subject to regulatory

approvals and approval by the boards of respective banks. Accordingly, Andhra Bank and Corporation Bank amalgamated into UBI w.e.f. April 01, 2020, with UBI being the anchor bank. The merged bank has a pan India network of 9,590 branches and 13,239 ATMs of June 30, 2020. The asset size of the merged bank stood at Rs.10,75,646 crore as on June 30, 2020, almost doubling in size as compared to the asset size of Rs.5,40,087crore (standalone) as on March 31, 2020, further increasing the stature of the bank. 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 FY20 (refers to period from April 01 to March 31), the bank received Rs.11,768 crore from GOI towards preferential allotment of equity shares, which helped the bank to report Capital Adequacy Ratio (CAR) (standalone) of 12.81% as on March 31, 2020 (P.Y.:11.78%), Tier I CAR of 10.75% (P.Y.:9.48%) and CET-1 Ratio of 9.40% (P.Y.:8.02%). Post-merger, the bank reported CAR of 12.01% (Tier I CAR: 9.74%) and Common Equity Tier I (CET I) ratios 8.60% as on April 01, 2020 as against minimum regulatory requirement of CAR of 10.875%, Tier I CAR of 8.875% and CET I ratio of 7.375%.

Post the merger, the bank shifted securities from HFT to AFS resulted in increase in the risk weighted assets (RWA) of the bank as on June 30, 2020. As a result, the bank reported CAR of 11.62% (Tier I CAR: 9.48%) and CET I Ratio of 8.40% as on June 30, 2020. Although, the bank has maintaining a steady trend of capitalisation levels over the years with periodic capital infusion by GOI; the capital adequacy ratio (CAR) as on June 30, 2020 were slightly moderate as compared to its peer public sector banks. Further, any stress in asset quality would require additional provisioning which would impact the capital adequacy levels of the bank. The bank has an enabling board resolution to raise capital funds of up to Rs.10,300 crore subject to equity capital not exceeding Rs.6,800 crore and Tier II bonds / AT I bonds not exceeding Rs.9,400 crore with necessary approvals. The envisaged infusion of equity would help the capital buffers of the bank in the near term and allow the bank to absorb any stress in asset quality and would remain a key rating sensitivity.

Stable resources profile and comfortable liquidity profile

The bank has an established liability franchise and a healthy deposit rollover rate and capital raising ability provide comfort. The bank expanded its deposit base post merger to Rs.8,92,542 crore as on June 30, 2020, as against Rs.4,50,668 crore as on March 31, 2020with Current Account Savings Account (CASA) proportion of 33.30% as on June 30, 2020 as compared to 35.59% (standalone) as on March 31, 2020.

The liquidity position of the bank was comfortable with well-matched asset liability maturity (ALM) profile as on March 31, 2020 with positive cumulative mismatches in all time buckets up to 5 years. The bank had excess SLR investments of Rs.68,233 crore as on March 31, 2020. The bank's Liquidity Coverage Ratio (LCR) stood at 185.42% as on March 31, 2020 (128.76% as on March 31 2019). Since April 01, 2020, the LCR is being computed on daily basis as per RBI guidelines for the amalgamated entity. The average LCR for the quarter ended June 30, 2020 is 163.84%, and is well above the minimum requirement as prescribed by RBI of 80% for the quarter ended June 30, 2020.

Moderate advances profile

During FY20, the bank saw credit growth at 6.10% with net advances of Rs.3,15,049 crore (standalone) as on March 31, 2020 as against Rs.296,932 crore as on March 31, 2019. The merged bank reported net advances of Rs.5,99,830 crore as on April 01, 2020 and Rs.5,81,717 crore as on June 30, 2020.As on March 31, 2020, the Retail, Agriculture and MSME (RAM) segment constituted 52% of total advances. Post-merger, the RAM segment constituted around 54% of total advances while large corporate & other advances constituted 46% of total gross advances as on June 30, 2020.

The retail loan portfolio grew from Rs.57,092 crore as on March 31, 2019 to Rs.60,519 crore as on March 31, 2020. Home loans, having the highest share in retail, grew by 4.34%. Priority sector advances constituted 44.93% of the Adjusted Net Bank Credit (ANBC) against the RBI mandate of 40%.

Key Rating Weaknesses

Moderate profitability parameters

During FY20, the bank reported a net loss of Rs.2,898 crore (standalone) as compared to net loss of Rs.2,948crore during FY19 and net loss of Rs.5,247 crore during FY18. While the operating profit increased by 22% during FY20, the credit costs of the bank remained at elevated levels over the last three years which has resulted in the bank reporting loss. During FY20, provisions stood at Rs.11,814 crore as compared to Rs.11,435 crore for the previous year.

UBI (amalgamated) reported Profit After Tax (PAT) of Rs.333 crore on total income of Rs.19,891 crore for the Q1FY21 (refers to period from April 01 to June 30) with operating profit of Rs.4,034 crore.

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%, 6.85% and 106.73% respectively. The amalgamation of Andhra Bank and Corporation Bank with Union Bank of India came into effect from April 01, 2020. Accordingly, the bank made a harmonization provisioning of Rs.3,655 crore in its books with regard to the impact of divergence in asset classification practices across the three banks as on March 31, 2020. (Rs.2,510 crore relating to UBI, Rs.200 crore relating to Corporation Bank and Rs.945 crore relating to Andhra Bank).
The bank reported GNPA, NNPA and Net NPA to Net-worth ratios of 14.15%, 5.49% and 74.62%, respectively, as on March 31, 2020 (on a standalone basis). Post-merger, the GNPA deteriorated to 14.66%, while the NNPA improved to 5.24%. PCR stood at 78.18%. As on June 30, 2020, the bank reported GNPA and NNPA ratios of 14.95% and 4.97% respectively. During FY20, the bank made a cash recovery of Rs.4,267 crore in addition to up gradation of accounts to the tune of Rs.1,871 crore. Provision Coverage Ratio (PCR) improved by 740 bps to 73.64% as on March 31, 2020 compared to 66.24% as on March 31, 2019. The bank has made a total provision towards IBC (Insolvency and Bankruptcy Code) accounts to the tune of Rs.6,940 crore, with a 99.5% coverage.

Liquidity Profile: Strong
The asset liability maturity (ALM) profile as on March 31, 2020 had positive cumulative mismatches in all the time buckets. The bank had excess SLR investments of Rs. 43169 crore as on March 31, 2020, 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.

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, which holds majority shareholding in the bank.

Applicable Criteria
Criteria on assigning Outlook and Creditwatch 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 Bank
Union Bank of India (UBI) was established in 1919. Government of India (GoI) is the majority shareholder holding 89.07% stake as on June 30, 2020.The Ministry of Finance (MoF), in consultation with Reserve Bank of India (RBI) on August 30, 2019, announced a set of reforms for public sector banks (PSBs) including consolidation, capital infusion and measures to improve governance standards. As part of consolidation, Andhra Bank and Corporation Bank were to be amalgamated into UBI with UBI being the anchor bank. The merger of the banks was effective April 01, 2020. As a part of the merger, shareholders of Andhra Bank got 325 equity shares of UBI of Rs.10 (face value) for every 1,000 equity shares of Rs.10 each of Andhra Bank and 330 equity shares of UBI of Rs.10 (face value) for every 1,000 equity shares of Rs.2 each of Corporation Bank. The merged has a pan India network of 9,590 branches and 13,239 ATMs of June 30, 2020. 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.

Brief Financials (Rs. crore)	March 31 2019 (A)	March 31, 2020 (A)
Total operating income	38,541	42,492
PAT	(2948)	(2,898)
Total Assets	4,86,602	5,40,152
Net NPA (%)	6.85	5.49
ROTA (%)	(0.61)	(0.56)

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.
Total Assets of the amalgamated bank as on April 1, 2020 are Rs.10,00,905 crore with Net NPA of 5.24%

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 assigned along with Outlook
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 ; Negative
Lower Tier II Bonds	INE692A09241	28-Dec-12	8.9%	28-Dec-22	800	CARE AA+ ; Negative
Basel III Compliant Perpetual Bonds (ATI Bonds)	INE692A08029	15-Sep-16	9.5%	Perpetual (call option after 10 years)	1,000	CARE AA- ; Negative
Basel III Compliant Perpetual Bonds (ATI Bonds)	INE692A08037	04-Nov-16	9%	Perpetual (call option after 5 years)	1,000	CARE AA- ; Negative

**Call option exercised on 29-Jun-20*

Annexure 2- Rating History of last three years

Sr. No.	Name of the Instrument	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.	Bonds-Upper Tier II	LT	-	-	-	1)Withdrawn (14-Feb-20) 2)CARE AA (Under Credit watch with Developing Implications) (07-Jan-20) 3)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)
2.	Bonds-Upper Tier II	LT	500.00	CARE AA; Negative	-	1)CARE AA (Under Credit watch with Developing Implications) (07-Jan-20) 2)CARE AA	1)CARE AA; Stable (02-Jan-19)	1)CARE AA; Stable (09-Oct-17)

						(Under Credit watch with Developing Implications) (11-Sep-19)		
3.	Bonds-Lower Tier II	LT	800.00	CARE AA+; Negative	-	1)CARE AA+ (Under Credit watch with Developing Implications) (07-Jan-20) 2)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)
4.	Bonds-Perpetual Bonds	LT	2000.00	CARE AA-; Negative	-	1)CARE AA- (Under Credit watch with Developing Implications) (07-Jan-20) 2)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)

Annexure-3: Complexity level of various instruments of Union Bank of India

Sr. No.	Name of the Instrument	Complexity Level
1.	Bonds-Lower Tier II	Complex
2.	Bonds-Perpetual Bonds	Highly Complex
3.	Bonds-Upper Tier II	Highly Complex

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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