September 24, 2020

State Bank of India – Ratings reaffirmed and withdrawn for various debt programmes

Summary of rating action

Instrument*	Previously Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Certificate of Deposits	41,500.00	0.00	[ICRA]A1+; Reaffirmed and withdrawn
Basel III Compliant Tier I Bonds	18,235.70	18,235.70	[ICRA]AA+(hyb)(Stable); Outstanding
	764.30	0.00	[ICRA]AA+(hyb)(Stable); reaffirmed and withdrawn
Basel III Compliant Tier II Bonds	22,243.00	22,243.00	[ICRA]AAA(hyb)(Stable); Outstanding
	500.00	0.00	[ICRA]AAA(hyb)(Stable); reaffirmed and withdrawn
Lower Tier II Bonds Programme	500.00	500.00	[ICRA]AAA(Stable); Outstanding
Medium Term Deposits	NA	NA	MAAA(Stable); Outstanding
Total	**84,743.00**	**40,978.70**	

** Instrument details are provided in Annexure-1*

Rationale

The rating for certificate of deposit programme of State Bank of India (SBI) has been reaffirmed and withdrawn as there is no amount outstanding against the rated programme. Additionally, of the rating on Rs 764.30 crore Basel III compliant Tier I bonds and Rs 500.00 crore Basel III compliant Tier II bonds, has been withdrawn as the bonds were not issued against the rated amount. The rating withdrawals are at the request of the bank.

The ratings on various instruments of SBI continue to be supported by its majority sovereign ownership and its status as a systemically important bank (SIB), given its dominant position in the Indian financial system. SBI has a dominant market share in Indian banking sector advances and domestic deposits at ~24%[1] each. The rating continues to reflect the steady growth in advances and the strong resource profile with a high share of the CASA deposits, leading to competitive cost of funds, high granularity in its deposit base, thus imparting superior liquidity. The bank has declared ~9.5% of its loan book under the moratorium[2], which has created an uncertainty on the asset quality in the near-term. The management has guided for a slippage of 1.5-1.6% of advances during FY2021, which in our view can be absorbed through its operating profits. In our view, given the high provisions on legacy stressed exposures and limited incremental ageing provisions, even in a stress scenario, the bank is well placed to absorb higher slippages of 2.5-3.0% through its operating profits. However, in such stress scenario, the internal capital generation of the bank will be muted and hence the bank may need to raise growth capital. While GoI has not budgeted any capital for public sector banks (PSBs) for FY2021, however, in our view, SBI's capital requirements are comfortable in relation to its market capitalisation levels and the bank has demonstrated strong ability to raise funds from the market in the past. The bank has enough headroom to raise the requisite capital

1 *As on March 31, 2020*
2 *Customers who have not paid one or no monthly loan installment during March-June 2020*

from market while maintaining GoI's shareholding at more than 51% level. Most of SBI's subsidiaries remain self-sufficient and profitable with limited incremental capital requirements in the medium term and offer considerable value-unlocking opportunities to SBI.

ICRA expects the bank will continue to benefit from its dominant position in the Indian banking industry, strong ability to raise capital, strong resource profile and sovereign ownership. While the near-term stress could emerge on asset quality because of Covid-19 induced pandemic, however this is expected to be absorbed through its operating profits driving stable outlook on the ratings.

Key rating drivers

Credit strengths

Systemically important bank with majority sovereign ownership – The ratings continue to factor in SBI's majority sovereign ownership (57.64% equity shares held by the Government of India (GoI) as on June 30, 2020) and the demonstrated capital infusion from the parent (total capital infusion of Rs. 19,874-crore during FY2016-2018 under recapitalisation plan). SBI also holds a dominant position in the Indian banking industry with a market share in banking sector advances and domestic deposits at ~24% each as on March 31, 2020 and market leadership in various product segments. Given SBI's dominance in the overall financial system, it has been classified as a Domestic Systemically Important Bank (D-SIB) by the RBI, which entails a higher capital requirement of 0.6% of risk weighted assets (RWAs) over the regulatory requirements. During FY2019 and FY2020, the GoI infused ~1.76 lakh crore in various PSBs[3], however, there was no capital infusion into SBI from the GoI during these periods as it was relatively better placed. Going forward, in ICRA's view, the bank will require growth capital in case of a scenario of stress on asset quality and profitability. Further, based on the existing GoI shareholding, SBI can raise enough capital for growth from the non-GoI sources while maintaining majority GoI ownership.

Strong market position across retail & corporates segment – SBI's standard loan book grew by ~7.7% YoY to Rs. 22.55 lakh crore as on June 30, 2020 up from Rs. 20.69 lakh crore as on June 30, 2019. The increase in advances was driven by a healthy credit off-take across the retail personal segment (12.85% YoY growth), while the growth in the agriculture and the SME segments remained subdued at 1.61% and -0.89%, respectively. The corporate loan book growth remained muted at 3.4% YoY as on June 30, 2020 because of a de-growth in certain segments like infrastructure, textiles, steel and petroleum products, even as it was offset by increased growth in the services segments. SBI holds a dominant position in the home loan and auto loan segments with a market share of over 32% each and an overall market share of 24% in advances of the Indian banking industry. As of June 30, 2020, SBI's domestic loan book was dominated by corporate advances which constituted 39.7% of the bank's gross advances followed by retail advances (excluding SME) at 36.7%, SME advances at 13.6% and agriculture advances at 10.0%. The international loan book constituted 14.4% of its gross advances (overall) as on June 30, 2020. Despite higher growth in retail advances, the share of the top 20 exposures and the share of the top 20 exposures as % of Tier 1 capital had inched up and stood at 13.93% and 233% as on March 31, 2020 (12.80% and 218% respectively as on March 31, 2019). The management has guided for a 6-8% credit growth in FY2021 and the same will be supported by a strong deposit base, planned capital raising and/or divestment of stake in non-core businesses in the near to medium term.

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[3] *Includes capital infusion in IDBI Bank Limited as well*

Strong resource profile and competitive cost of funds – Supported by its large branch network across India as well as the large share in Government business and well-developed customer franchise, SBI holds a dominant position in the Indian banking industry with a ~24% market share in deposits as at March 31, 2020. Despite its high market share of deposits, the share of the top 20 depositors stood the lowest amongst other PSBs at 2.94% as on March 31, 2020 (3.11% as on March 31, 2019). SBI's current account and saving account (CASA)-to-deposits (domestic) ratio remains one of the highest amongst the PSBs, which is supported by a large pool of Rs 14.98 lakh crore of low-cost CASA deposits, a significant credit positive, translating into lower cost of interest-bearing funds. The bank's domestic CASA deposits ratio stood at 45.34% as on June 30, 2020 compared to the PSBs average of ~39.7%. The CASA deposits continue to register a strong YoY growth of ~16.7% in Q1 FY2021, much higher than ~7-8% YoY growth for the PSBs as on March 31, 2020. For Q1 FY2021, the cost of interest-bearing funds stood at 4.37% (4.85% for Q1 FY2020) against the PSB average of 4.86% in Q4FY2020. Going forward, ICRA expects the strong liability profile of SBI to continue to remain a significant positive to support its credit growth, while maintaining liquidity and profitability.

Adequate capital position with sizeable value unlocking opportunities from non-core businesses – The bank has last raised an equity capital of Rs 15,000 crore in FY2018, in addition to which it also received an equity capital of Rs 8,800 crore from GoI as part of PSBs recapitalisation. Over the last two years (FY2019 and FY2020), the bank has managed to grow its net advances by ~20% without fresh equity capital raise mainly through a calibrated growth in RWAs by focusing on retail assets and better rated corporate exposures. The bank has also raised ~Rs 14,000 crore though issuance of Tier 1 bonds during past two years. While GoI has not budgeted any capital for PSBs for FY2021, ICRA expects SBI is well positioned to raise requisite capital from markets, if required. The bank secured shareholder approval for raising equity capital of up to Rs 20,000 crore during FY2021, however, the capital raising is likely to be dependent on the trends in asset quality and consequent impact on internal capital generation after the moratorium ends. In a scenario of higher slippage, ICRA expects that the bank could require capital for achieving growth in advances.

The bank's standalone capitalisation profile remains comfortable (CET1 of 10.14%, Tier 1 of 11.35% and CRAR of 13.40%) as on June 30, 2020 against the regulatory requirement[4] of 8.60%, 10.10% and 12.10% respectively as on September 30, 2020. On consolidated basis, the capital ratios remain better than standalone basis with CET 1 of 10.95%, Tier 1 of 12.12% and CRAR of 14.13% as on June 30, 2020 mainly because of better capitalisation profile for most of the subsidiaries.

Further, In ICRA's view, SBI's subsidiaries are largely remain self-sufficient in meeting their capital requirements in the near to medium term. The CET1 of the bank has not gone below 9.57% during the last four years and ICRA expects, the bank will continue to maintain capital cushions of over 1% above the regulatory capital requirements at a consolidated level while pursuing growth.

SBI, through its various subsidiaries, offers various other financial services like asset management, life insurance, general insurance, credit cards, capital markets and various other services, including stakes in various regional rural banks. SBI also has banking operations in other countries through various overseas subsidiaries. Some of these businesses have been fairly scaled over a period and are among the leading players in their industry segments. During FY2018, SBI divested its stake in SBI Life Insurance Limited, resulting in a profit of Rs. 5,436 crore and during FY2019, SBI divested its stake in the general insurance business to raise Rs 473 crore and Rs 1,087 crore from part

[4] *Including capital conservation buffer of 2.5% of risk weighted assets (RWAs) and 0.60% of RWA for being a D-SIB*

divestment of its merchant acquisition business. In FY2020, the bank further divested 4.5% stake in SBI Life Insurance Limited, resulting in a profit of Rs. 3,484 crore and 4.4% stake in SBI cards and payment services limited for a profit of Rs 2731 crore. During Q1FY2021, SBI further sold 2.1% stake in SBI Life for a profit of Rs 1367 crore. SBI may divest its stake in a few more businesses in near term to unlock the value of its subsidiaries and will also aid the profits and capital levels of the bank.

Credit challenges

Uncertainty on asset quality given the Covid induced moratorium on loan book – SBI's asset quality has been on improving trend since the merger of its various subsidiaries and associated banks effective from April 1, 2017. Consequently, its GNPAs and net NPAs (NNPAs) has declined to 6.15% and 2.23% as on March 31, 2020 as compared to 9.98% and 5.97% respectively as on June 30, 2017. The fresh slippage rate remained moderate to ~2.6% of standard advances during FY2020 (2.2% in FY2019 and 5.5% in FY2018). The stock of SMA[5]-1 & 2 accounts remained limited at Rs 1,750 crore (<0.1% of standard advances) as on June 30, 2019, compared to ~Rs. 18,313-crore (0.88% of standard advances) as on September 30, 2019 reflecting improvement in asset quality. The bank has high provision cover (including write offs) of 83.62% as on June 30, 2020 on its Gross NPAs and this will drive limited incremental credit provisions of 50-60 bps annually for the bank till FY2022. However, with the Covid-19 induced pandemic and subsequent moratorium granted by the bank on loan repayments by its customers, the uncertainty on asset quality has increased in near-term.

The bank has declared ~9.5% of its loan book under the moratorium as on June 30, 2020 (down from ~18% at May-end), which has created an uncertainty on the asset quality in the near-term. Though the management has guided for a slippage of 1.5-1.6% of advances during FY2021, however given a sharp deceleration in economic growth, a higher stress cannot be ruled out. Additionally, Reserve Bank of India (RBI) has also allowed banks to restructure the loans impacted by Covid-19 which could reduce near-term slippages but create uncertainty in future on such restructured accounts.

In our view, given the high provisions on legacy stressed exposures and limited incremental ageing provisions, even in a scenario of higher slippages of 2.5-3.0%, the credit cost (Credit provision/Average Total Assets - ATA) to be at ~1.2-1.3% for FY2021 which can be absorbed through its operating profits. However, this may result in limited reduction or a marginal increase in net NPAs from a level of 2.23% on March 31, 2020.

Well placed to absorb credit costs through operating profits but could drive muted profitability – Supported by competitive cost of interest bearing funds, improved asset quality and lower slippages leading to lower interest reversals, the operating profit (before divestments and trading income) has been improving to 1.57% of ATA during FY2020 (1.54% during FY2019 and 1.41% during FY2018). With declining fresh slippages and improved provision cover, the credit costs to ATA have also been declining to 1.13% during FY2020 (1.51% in FY2019 and 2.00% in FY2018). This has been further supported by the divestment of stake in subsidiaries, translating in improved net profits. The Return on assets (RoA) improved to 0.38% in FY2020 (0.02% in FY2019 and -0.20% in FY2018).

Going forward, given the uncertainty on asset quality, the outlook on profitability remains uncertain, however with limited incremental provisions on legacy stressed assets, ICRA expects the bank to absorb the credit provisions

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[5] *Special Mention Account; SMA 1 is overdue by 31-60 days and SMA 2 is overdue by 61-90 days. The exposure to SMA accounts of SBI with exposure of >Rs 5 crore*

through its operating profits in a scenario of slippages guided by the management as well as our scenario of higher slippage. In case the slippages remain range-bound at 1.5-1.6% guided by the management, we expect the RoA and RoE to be ~0.4% and ~7%, which may be sufficient to support the 6-8% credit growth without need for fresh capital. However, if the slippages were to be higher at 2.5-3.0%, the RoA and RoE could moderate to ~0.1% and 1.5-2.0%, which will require bank to raise capital for growth.

Liquidity position - Superior

Supported by its strong retail liability franchise, excess SLR holdings of ~7.5% of net demand and time liabilities during FY2020, and a strong liquidity coverage ratio of 151.30% for quarter ending June 30, 2020 as against the regulatory requirement of 100% as on January 1, 2019 onwards. ICRA expects SBI to maintain a superior liquidity, given its large proportion of retail deposits and high portfolio of liquid investments. The bank can also avail of liquidity support from the RBI (through reverse repo against excess SLR investments and marginal standing facility mechanism) in case of urgent liquidity needs.

Rating sensitivities

Positive triggers – Not applicable

Negative triggers – Given the dominant position of SBI in the Indian financial sector and its sovereign ownership, ICRA expects SBI to continue to maintain sufficient capitalisation over regulatory levels. While a net solvency weaker than 40% on a sustained basis could be a credit negative for the bank. ICRA expects continued extraordinary support from the GoI, if required given its systemic importance and any dilution in the stance will also be credit negative.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA Rating Methodology for Banks Impact of Parent or Group Support on an Issuer's Credit Rating ICRA Policy on Withdrawal and Suspension of Credit Rating
Parent/Group Support	The rating factors in SBI's sovereign ownership and demonstrated track record of capital infusion by the GoI. ICRA expects the GoI to support SBI with capital infusion, if required.
Standalone/Consolidated	For arriving at the rating, ICRA has considered the standalone financials of SBI. However, in line with our limited consolidation approach, we have factored in the capital requirement of the key subsidiaries and overseas branches of the Group, going forward. In ICRA's view, SBI's subsidiaries will largely remain self-sufficient in meeting their capital requirements in the near to medium term.

About the company

The origin of the State Bank of India goes back to the 19th century with the establishment of the Bank of Calcutta in 1806 (redesigned as the Bank of Bengal in 1809), the Bank of Bombay (1840) and the Bank of Madras (1843). These three banks were amalgamated as the Imperial Bank of India in 1921. In 1951, when the country's first Five-Year Plan was launched, the Imperial Bank of India was integrated with other state-owned and state associated banks. An Act was accordingly passed in Parliament in May 1955 and the State Bank of India (SBI) was constituted in July 1955. Later, the State Bank of India (Subsidiary Banks) Act was passed in 1959, enabling SBI to take over seven former state-associated banks as its subsidiaries. Further, State Bank of Saurashtra was merged with SBI in 2008 and State Bank of Indore in 2010. On April 1, 2017, SBI was merged with five of its associate banks (State Bank of Bikaner and Jaipur, State Bank of Hyderabad, State Bank of Mysore, State Bank of Patiala and State Bank of Travancore) and Bharatiya Mahila Bank. The Government of India held 57.64% stake in the bank as on June 30, 2020. The bank has the largest network of 22,135 branches across India (as on June 30, 2020) and a significant overseas presence.

Key financial indicators – Standalone

	FY2019	FY2020	Q1 FY2020	Q1 FY2021
Net interest income – Rs Crore	88,349	98,085	22,939	26,642
Profit before tax – Rs Crore	1,607	25,063	4,063	5,560
Profit after tax – Rs Crore	862	14,488	2,312	4,189
Net advances – Rs Lakh Crore	21.9	23.3	21.3	23.0
Total assets (Excl revaluation reserves) – Rs Lakh crore	36.6	39.3	35.6	40.9
% CET 1	9.62%	9.77%	9.61%	10.14%
% Tier 1	10.65%	11.00%	10.65%	11.35%
% CRAR	12.72%	13.06%	12.89%	13.40%
% Net interest margin / Average total assets	2.23%	2.59%	2.54%^	2.66%^
% Net profit / Average total assets	0.02%	0.38%	0.26%^	0.42%^
% Return on net worth	0.44%	7.18%	4.71%^	7.97%^
% Gross NPAs	7.53%	6.15%	7.53%	5.44%
% Net NPAs	3.01%	2.23%	3.07%	1.86%
% Provision coverage excl. technical write offs	61.86%	65.21%	61.05%	67.07%
% Net NPA/ Core capital	35.55%	25.91%	35.03%	20.90%

^ ratios are annualised; FY2019 and FY2020 financials are audited and Q1FY2020 and Q1FY2021 financials are unaudited
All ratios are as per ICRA calculations.
Source: SBI; ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Type	Current Rating (FY2021)					Rating History for past 3 years					
			Amount Rated (Rs crore)	Amount Outstanding (Rs crore)	FY2021			FY2020		FY2019		FY2018	
					24-Sep-20	16-Sep-20	1-Sep-20	11-Nov-19	16-Aug-19	28-Feb-19	6-Jun-18	18-Jan-18	3-Oct-17
1	Certificate of Deposits Programme	ST	41,500	0.00	[ICRA]A1+; reaffirmed and withdrawn	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
2	Basel III Compliant Tier II Bonds Programme	LT	500.00	0.00	[ICRA]AAA(hyb) (Stable); reaffirmed and withdrawn	[ICRA]AAA (hyb) (Stable)	[ICRA]AAA (hyb) (Stable)	[ICRA]AAA (hyb) (Stable)	[ICRA]AAA (hyb) (Stable)	[ICRA]AAA (hyb) (Stable)	[ICRA]AAA (hyb) (Stable)	[ICRA]AAA (hyb) (Stable)	[ICRA]AAA (hyb) (Stable)
3	Basel III Compliant Tier I Bonds Programme	LT	764.30	0.00	[ICRA]AA+ (hyb)(Stable); reaffirmed and withdrawn	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	-
4	Basel III Compliant Tier II Bonds Programme	LT	7,000.00	-	[ICRA]AAA(hyb) (Stable); outstanding	[ICRA]AAA(hyb) (Stable); assigned	-		-	-	-	-	-
5	Basel III Compliant Tier I Bonds Programme	LT	18,235.70	18,235.70	[ICRA]AA+ (hyb)(Stable); outstanding	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	[ICRA]AA+ (hyb) (Stable)	-
6	Basel III Compliant Tier II Bonds Programme	LT	15,243.00	15,243.00	[ICRA]AAA (hyb)(Stable)	[ICRA]AAA (hyb)(Stable)	[ICRA]AAA (hyb)(Stable)	[ICRA]AAA (hyb)(Stable)	[ICRA]AAA (hyb)(Stable)	[ICRA]AAA (hyb)(Stable)	[ICRA]AAA (hyb)(Stable)	[ICRA]AAA (hyb)(Stable)	[ICRA]AAA (hyb)(Stable)
7	Lower Tier II Bonds Programme	LT	500.00	500.00	[ICRA]AAA (Stable); outstanding	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
8	Term Deposits Programme	MT	NA	NA	MAAA (Stable); outstanding	MAAA (Stable)	MAAA (Stable)	MAAA (Stable)	MAAA (Stable)	MAAA (Stable)	MAAA (Stable)	MAAA (Stable)	MAAA (Stable)

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument Details

ISIN No	Instrument Name	Issuing Bank	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Basel III Compliant Tier II Bonds Programme	SBI	Proposed	-	-	7,000.00	[ICRA]AAA(hyb) (Stable)
INE062A08249	Basel III Compliant Tier I Bonds Programme	SBI	9-Sep-20	7.74%	09-Sep-25#	4,000.00	[ICRA]AA+(hyb) (Stable)
INE062A08223		SBI	22-Nov-19	8.50%	22-Nov-24#	3,813.60	
INE062A08199		SBI	22-Mar-19	9.45%	22-Mar-24#	1,251.30	
INE062A08173		SBI	4-Dec-18	9.56%	4-Dec-23#	4,021.00	
INE062A08181		SBI	21-Dec-18	9.37%	21-Dec-23#	2,045.00	
INE062A08215		SBI	30-Aug-19	8.75%	30-Aug-24#	3,104.80	
INE062A08074	Basel III Compliant Tier II Bonds Programme	SBI	2-Jan-14	9.69%	2-Jan-24	2,000.00	[ICRA]AAA(hyb) (Stable)
INE062A08082		SBI	23-Dec-15	8.33%	23-Dec-25	4,000.00	
INE062A08090		SBI	18-Feb-16	8.45%	18-Feb-26	3,000.00	
INE062A08108		SBI	18-Mar-16	8.45%	18-Mar-26	3,000.00	
INE062A08116		SBI	21-Mar-16	8.45%	21-Mar-26	500.00	
INE652A08015		SBoP	22-Jan-15	8.29%	22-Jan-25	950.00	
INE648A08013		SBBJ	20-Mar-15	8.30%	20-Mar-25	200.00	
INE649A08029		SBH	30-Dec-15	8.40%	30-Dec-25	500.00	
INE649A08037		SBH	8-Feb-16	8.45%	8-Feb-26	200.00	
INE649A09126		SBH	31-Mar-15	8.32%	31-Mar-25	393.00	
INE651A08041		SBM	31-Dec-15	8.40%	31-Dec-25	300.00	
INE651A08058		SBM	18-Jan-16	8.45%	18-Jan-26	200.00	
NA	Basel III Compliant Tier II Bonds Programme	SBI	-	-	-	500.00	[ICRA]AAA(hyb) (Stable); reaffirmed and withdrawn
INE648A09078	Basel II Compliant Lower Tier II Bonds Programme	SBBJ	20-Mar-12	9.02%	20-Mar-22	500.00	[ICRA]AAA (Stable)
NA	Medium Term Deposits Programme		-	-	-	-	MAAA(Stable)
NA	Certificate of Deposits Programme		-	-	7-365 days	41,500.00	[ICRA]A1+; reaffirmed and withdrawn
NA	Basel III Compliant Tier I Bonds Programme	SBI	-	-	-	764.30	[ICRA]AA+(hyb) (Stable); reaffirmed and withdrawn

Source: SBI; # First call option date

SBoP – State Bank of Patiala, SBBJ – State Bank of Bikaner and Jaipur, SBM – State bank of Mysore, SBoT – State Bank of Travancore, SBH – State Bank of Hyderabad

The rated Basel III-compliant Tier I bonds (or Additional Tier I or AT-I bonds) have the following loss absorption features that make them riskier:

- Coupon payments are non-cumulative and discretionary, and the bank has the full discretion at all times to cancel coupon payments. Cancellation of discretionary payments shall not be an event of default.

- Coupons can be paid out of the current year profits. However, if the current year's profit is not sufficient, or, if the payment of coupon is likely to result in a loss, the coupon payment can be done through reserves and surpluses[6] created through appropriation of profits (including statutory reserves). However, the coupon payment is subject to the bank meeting the minimum regulatory requirements for CET I, Tier I and total capital ratios (including capital conservation buffer, CCB) at all times as prescribed by the Reserve Bank of India (RBI) under the Basel III regulations.

These Tier I bonds are expected to absorb losses through the write-down mechanism at the objective pre-specified trigger point fixed at the bank's (CET-I) ratio as prescribed by the RBI – 5.5% till September 2020, and thereafter 6.125% of the total risk weighted assets (RWA) of the bank or when the Point of Non-Viability trigger is breached in the RBI's opinion.

The letters 'hyb' in parenthesis suffixed to a rating symbol stands for 'hybrid', indicating that the rated instrument is a hybrid subordinated instrument with equity-like loss-absorption features, which may translate into higher levels of rating transition and loss severity vis-à-vis conventional debt instruments.

Given the above distinguishing features of the Tier I bonds, ICRA has assigned a one notch lower rating on these than the rating on the Tier II instruments. The distributable reserves that can be used for servicing the coupon in a situation of inadequate profits or a loss during the year, stood at a comfortable at 6.3% of risk-weighted assets (RWA) as on March 31, 2020. The rating on the Tier I bonds continues to be supported by the bank's capital profile (CRAR: 13.40%; CET-I capital: 10.14% and Tier I capital: 11.35% as on June 30, 2020) which is likely to remain comfortable, given SBI's strong capital-raising ability as well as its systemic importance in the Indian banking system. The rating on the Basel III compliant Tier I bonds also factors in the uncertainty on the bank's profitability that may arise given the uncertainty on asset quality amid Covid-19 pandemic induced stress on asset quality. However, the same is expected to be absorbed through strong operating profits of the bank, buffer in existing capital levels and sizeable distributable reserves for servicing of these Tier I bonds.

[6] Calculated as per the amendment in Basel III capital regulations for AT-I bonds by the RBI, vide its circular dated February 2, 2017. As per the amended definition, distributable reserves include all reserves created through appropriation from profit and loss account.

ANALYST CONTACTS

Karthik Srinivasan
+91 22 6114 3444
karthiks@icraindia.com

Hemant Sultania
+91 124 4545 300
hemant.sultania@icraindia.com

Anil Gupta
+91 124 4545 314
anilg@icraindia.com

Aashay Choksey
+91 22 6114 3430
aashay.choksey@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 2556 0194/ 6606 9999

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