IDFC FIRST Bank Ltd

October 03, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term instruments	1,874.68 (Reduced from 3,194.78)*	CARE AA+; Stable	Revised from CARE AA; Stable

Details of instruments/facilities in Annexure-1. **amount reduced on account of redemption*

Rationale and key rating drivers

The revision in the rating assigned to the long-term debt instruments of IDFC FIRST Bank Limited (IDFC FIRST) factors in continued improvement in the scale of operations of the bank along with diversification and granularization of the advances book with a shift towards retail lending and gradual reduction in the legacy infrastructure lending coupled with growth of the liabilities franchise with increase in the proportion of the retail term deposits and current account savings account (CASA) deposits post the merger of erstwhile Capital First Limited (CFL) with erstwhile IDFC Bank Limited (IDFC Bank).

The rating also factors in the comfortable capitalization levels maintained by the bank due to regular capital raising undertaken to support its asset growth, improvement in earnings profile with granularization of the advances and reduction in cost of borrowings helping expansion of margin and decline in credit cost along with improvement in asset quality parameters during FY23 (refers to the period April 01 to March 31) and Q1FY24 (April 01 to June 30) post revival from the Covid-19 pandemic.

The rating is constrained on account of the challenges in asset quality of its legacy infrastructure advances against which the bank continues to maintain adequate provisions, however, the bank has witnessed significant improvement in the asset quality during FY23 and Q1FY24 with lower slippages and write-offs. Although, the proportion of unsecured lending continues to remain on the higher side, CARE Ratings Ltd (CARE Ratings) expects the bank to sustain the improvement in its asset quality with increasing granularization of advances and remains a key monitorable for the bank.

Further, the rating factors in the bank's relatively higher cost of borrowings partly due to legacy borrowings which continues to form a sizeable proportion of its funding profile, albeit on a decreasing trend and higher operating costs compared to peer banks due to the scale up of the retail franchise. Although, the bank has been focusing on rationalising the cost, a sustained improvement in cost remains critical to enable the bank to become more competitive in secured and price sensitive retail loan segments like Home Loans and LAP as well as large corporate segments keeping ticket sizes under check. Further, the bank remains to be relatively smaller in size in comparison to peer private sector banks.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors: Factors that could lead to positive rating action/upgrade

- Sustainable improvement in the market positioning and resource profile with a higher share of retail deposits
- Improvement in operating performance and improvement in the cost to income ratio

Negative factors: Factors that could lead to negative rating action/downgrade

- Higher-than-expected deterioration in the asset quality, with the gross non-performing assets (GNPA) level increasing to above 5% and thereby impacting the earnings profile
- Deterioration in the capitalisation levels with cushion over the minimum regulatory requirement of less than 3.5%
- Decline in the Return on Total Assets (ROTA) below 1%

Analytical approach: Standalone

Outlook: Stable

The stable outlook takes into consideration the comfortable capitalization levels, diversification and granularization in the advances book with higher proportion of retail advances, diversification in the resource profile with higher proportion of retail deposit base coupled with improved asset quality parameters and financial performance.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Detailed description of the key rating drivers:

Key strengths

Comfortable capitalization with demonstrated ability to raise capital

The bank has been maintaining comfortable capitalisation levels to support the growth in business as well as to have cushion to absorb credit costs. IDFC FIRST demonstrated its ability to raise capital over the last 3 years. During FY23, the bank raised equity capital of ₹2,196 crore via preferential allotment of equity shares following the equity capital raise of ₹3,000 crore during FY22 via qualified institutional placement (QIP) of equity shares. In addition, the bank also raised Tier II bonds of ₹1,500 crore each during Q1FY24, FY23 and FY22.

The bank reported Capital Adequacy Ratio (CAR) of total CAR of 16.82% and Tier I CAR (entirely CET-I) of 14.20% as on March 31,2023 (March 31,2022: CAR: 16.74%, Tier I CAR: 14.88%), which is over and above the regulatory requirement of 11.5% and 9% respectively. As on June 30,2023, the total CAR stood at 16.96% and Tier I CAR stood at 13.70%. The current capitalisation level is comparable to peer mid-sized private sector banks, albeit lower than larger sized peers.

The bank has enough capital cushion in the near term to support the business growth and has an internal threshold to maintain CET-I of over 13% and CARE Ratings expects the bank to raise capital periodically to fund its planned growth and maintain comfortable capitalisation levels.

Increasing diversification and granularization of advances with a shift towards retail lending

Post the merger of IDFC Bank with CFL in December 2018, the bank has been focussed in diversifying its advances book with increase in the retail and commercial advances and gradually moderating and balancing the corporate lending book with steady decline in infrastructure lending book. Further, the bank's retail book has a diversified product mix including home loans, loan against property (LAP), SME loans, vehicle loans, consumer durable loans and the bank has entered into credit cards from FY21.

During FY23, the bank witnessed a growth of 24% in the advances book (including credit substitutes and net of IBPC) against the industry credit offtake of 15%. The gross advances book (including credit substitutes and net of IBPC) stood at ₹1,60,599 crore as on March 31,2023 as compared ₹1,29,051 crore as on March 31,2022. The bank has made consistent investments in increasing the retail base with shift towards granular retail lending. Out of the total advances, the retail book constituted 69% as on March 31,2023 as against 9% as on March 31, 2018.

As a strategy, the bank has been increasing the proportion of the retail business as the bank has witnessed low NPA in these segments. The proportion of the retail advances (including commercial finance) has increased to around 79% of total advances as on March 31,2023 (March 31, 2022: 72%) and remained at 79% as on June 30,2023

Within retail, the mortgage loans book consisting of home loans and LAP constitutes highest share of 23% followed by consumer loans of 14%, rural finance of 12% as on June 30,2023. The growth in the rural finance is primarily driven by strong growth in Kisan Credit Cards (KCC), tractor loans, and steady growth in microfinance through joint liability group (JLG) portfolios, which contribute around 55% of the overall rural portfolio as on March 31,2023.

The wholesale funded assets have decreased from around ₹53,614 crore with infrastructure lending book of ₹21,459 crore as on March 31, 2019, to around ₹31,421 crore with infrastructure lending book of ₹3,758 crore as on June 30, 2023. The concentration in the wholesale advances has also reduced over the last few years. The advances to top 20 borrowers declined from 111% of tangible net worth as on March 31, 2021, to 64% of tangible net worth as on March 31, 2023.

The bank plans to be predominantly retail focused with retail lending (including commercial finance) constituting over 70% of total advances going forward as the legacy infrastructure lending book would run down in medium term.

Diversification in the resource profile

The total deposits of the bank have seen a significant growth over the last few years with 37% growth during FY23. As on March 31,2023, the total deposits stood at ₹1,44,637 cr (March 31,2022: ₹1,05,634 crore) and further to ₹1,54,427 crore as on June 30, 2023. The CASA deposits witnessed a growth of 41% and the term deposits witnessed a growth of 33% during FY23. The proportion of CASA deposits stood at 49.77% of total deposits as on March 31, 2023, and at 46.47% of total deposits as on June 30, 2023, witnessing a substantial improvement from 12.93% as on March 31, 2019. With growth in the deposit franchise of the bank, the credit to deposit ratio has improved from 125% as on March 31, 2019, to 107% as on June 30, 2023. Going forward, with the increase in the deposit base, the credit to deposit ratio is expected to improve further to be in line with the peers.

The term deposits (including certificate of deposits) grew by 33% during FY23 with the proportion of retail customer deposits to total customer deposits increasing from 73% as on March 31, 2022, to 76% as on March 31,2023. Further, the proportion of retail customer deposits increased to 77% as on June 30,2023.The ability of the bank in maintaining a stable CASA base and retail deposits on a sustainable basis and bringing down the cost of deposit would be a key monitorable for the bank.

The bank has been able to reduce the high-cost borrowings over the last few years which stands at ₹16,055 crore as on June 30,2023 as compared to ₹22,406 crore as on June 20, 2022. While the bank had offered higher interest rate to garner deposits to increase its depositor base as compared to the peers, in May 2021, the bank reduced the interest rate on deposits upto ₹10 lakhs from 7% to 4%, and the bank continued to see rise in overall deposits by 37% in FY23. However, with the increase in the deposit base along with run-down in the high-cost borrowings over the next 2 years, the cost of funds is expected to stabilize. Further, the bank has option to raise refinance from development finance institutions to rationalize its cost of funds in the near term.

Key weaknesses

Moderate profitability, albeit improvement

During FY23, the bank witnessed improvement in the earnings profile owing to favourable economic environment, rising interest rate scenario leading to improved net interest margin (NIM) and asset quality. The NIM of the bank stood at 5.92% during FY23 (FY22: 5.56%) due to increase in the high yielding retail book which comprises majorly home loans, LAP, rural finance, consumer loans and so on and rising interest rate scenario during FY23. Out of the total advances, around 40% of the book are based on floating interest rate, and out of which 60% are linked to repo. As repo rate witnessed 250bps rise during FY23, the yield on advances has increased coupled with slower pace of repricing of deposits. The operating expense as a % of total assets stood at 5.70% during FY23 (FY22: 5.52%) led by increase in the branches, employee strength and majorly involves cost incurred in increasing the granular retail base. During FY23, the bank increased the branch network to 809 with addition of 168 branches during the year and employee strength to 35,352 with an addition of 7548 employees. The credit costs stood at 0.78% during FY23 which improved from 1.78% during FY22 led by better asset quality performance and stringent underwriting policies of the bank. During FY22, the bank had maintained higher provisions for the retail loan book owing to COVID-19. On account of which, ROTA improved to 1.14% during FY23 as compared to 0.08% during FY22. During Q1FY24, the NIM (annualised) stood at 6.15% (Q1FY23: 5.66%) and ROTA stood at 1.26% (Q1FY23: 1.03%).

Going forward, the operating expenses are expected to remain high as the bank continues to expand its reach in the retail base, however, the same would be offset by the increasing high yield retail loan book. The credit costs are expected to remain range bound. As the business scales up, the operating efficiency is expected to improve with the ROTA of around 1.5% in the medium term.

Improvement in asset quality parameters

The asset quality of the bank has observed improvement during FY23 owing to recovered economic environment post pandemic related stress and better collection efforts.

As on March 31,2023, the asset quality improved with GNPA and Net NPA (NNPA) at 2.51% and 0.86% respectively as compared to GNPA and NNPA at 3.70% and 1.53% as on March 31,2022. The slippage ratio has also improved to 3.90% as on March 31,2023 from 7.60% as on March 31,2022. The net stressed asset (Net NPA+ Net Restructured Assets+ Net Security Receipts) to tangible net worth ratio also improved to 8.38% as on March 31,2023 (March 31,2022: 22.05%). Further improvement was witnessed during Q1FY24 with GNPA at 2.17% and NNPA at 0.70% as on June 30,2023.

The bank has witnessed substantial growth in the retail book over the last few years. Although, the bank has disclosed the collection efficiency on the retail book which stood at around 99.2% to 99.5% all through FY23 and the latest collection efficiency at 99.5% which provides comfort, the asset quality performance would be a key rating monitorable. Further, to mitigate the credit risk in newly originated book, the bank has maintained adequate provision coverage ratio (including technical write offs) of 80.29% as on March 31, 2023 (March 31,2022: 70.29%).

Liquidity: Adequate

According to the asset liabilities maturity (ALM) profile as on June 30, 2023, the bank had no negative cumulative mismatches in the time bucket for up to one year.

The liquidity position of the bank stood strong with quarterly liquidity coverage ratio of 125.64% as on June 30,2023, as against the minimum regulatory requirement of 100%. The bank maintained high quality liquid assets of ₹42,336 crore as on quarter ended June 30,2023 as against ₹37,299 crore maintained for quarter ending March 31,2023.

The bank manages its deposit maturities in a particular time bucket by appropriately modifying the deposit rates. Furthermore, the bank has access to systemic liquidity like the Reserve Bank of India's (RBI's) liquidity adjustment facility (LAF) and marginal standing facility (MSF) along with access to refinancing from the Small Industries Development Bank of India (SIDBI), the National Housing Bank (NHB), the National Bank for Agriculture and Rural Development (NABARD), etc, and access to call money markets.

Environment, social, and governance (ESG) risks

The bank has in place a dedicated governance structure, starting with a Board Committee that manages Stakeholders' Relationship, ESG and Customer Service (SRECS), which in turn, is supported by an ESG Management Committee and a Working Group. The ESG function is responsible for identifying opportunities for the Bank to create a larger impact; acting as a centre of excellence for all ESG initiatives across the Bank; running point on ESG goals; evaluating ESG risks; and communicating to stakeholders on the Bank's ESG progress through benchmarked reporting.

The bank has financed over 1.2 lakh units (Rs. 1160 crore) in EV sales in FY23 compared to 20,000+ units in FY22. The bank follows Equator Principles, which is credit risk management framework for identifying, assessing, and managing environment and social risk for project finance. The bank focusses on financial inclusion as a part of its social objective. The bank has opened rural bank branches with focus on lending to Small & Marginal Farmers and customers with annual income below ₹2.5-3 lakhs. Around 71% of the borrowers of the rural portfolio are women. The bank had held 134 sessions of holistic employee wellbeing programmes covering physical, mental, and financial health. The bank has 60% of the board consisting of independent directors, thus ensuring transparency. Also, the bank had zero penalties for non-disclosure during FY23.

Applicable criteria

Policy on default recognition
Financial Ratios - Financial Sector
Rating Outlook and Credit Watch
Bank
Policy on Withdrawal of Ratings

About the company and industry

Industry classification

Macro Economic Indicator	Sector	Industry	Basic Industry
Financial Services	Financial Services	Banks	Private Sector Bank

IDFC FIRST was incorporated in October 2014 and the name of the bank underwent a change from 'IDFC Bank Limited' (IBL) to 'IDFC FIRST Bank Limited' with effect from January 12, 2019, following the merger of Capital First Limited with the bank. The merger of Capital First Limited and its two subsidiaries with IDFC Bank Limited has become effective from December 18, 2018. IDFC Ltd holds 39.93% stake in IDFC FIRST. The bank's operations are spread across its three business verticals: corporate banking, consumer banking and rural banking. As on June 30, 2023, it has a network of 824 branches and 1,069 ATMs across the country. The bank is led by MD-CEO, Mr. V. Vaidyanathan, who has over 25 years of banking experience across Citibank and ICICI Bank Group. The appointment of the MD-CEO is approved by RBI until December 2024.

IDFC FIRST made an announcement on stock exchanges dated July 03, 2023, that the Board of Directors of IDFC FIRST, at its meeting held on July 03, 2023, has inter alia, approved the composite Scheme of Amalgamation (Scheme) amongst 'IDFC Financial Holding Company Limited' (IFHCL) and 'IDFC Limited' and the Bank, and their respective shareholders, under Sections 230 to 232 of the Companies Act, 2013 and other applicable laws including the rules and regulations which envisages (i) the amalgamation of (a) IFHCL into and with IDFC Limited; and (b) IDFC Limited into and with the Bank, and (ii) reduction of securities premium account of the Bank. The Share Exchange Ratio for the amalgamation of IDFC Limited into and with IDFC First Bank shall be 155 equity shares (credited as fully paid-up) of face value of ₹10/- each of IDFC FIRST for every 100 fully paid-up equity shares of face value of ₹10/- each of IDFC Limited. As a result of the proposed merger, the standalone book value per share of the Bank would increase by 4.9%, as calculated on audited financials as of March 31, 2023. IDFC Limited and IFHCL have negligible operations.
The Scheme is subject to the receipt of requisite approvals from the Reserve Bank of India (RBI), Securities and Exchange Board of India (SEBI), the Competition Commission of India, the National Company Law Tribunal, BSE Limited and the National Stock Exchange of India Limited.

Brief Financials (₹ crore)	March 31, 2022 (A)	March 31, 2023 (A)	Q1FY24 (UA)
Total income	20,395	27,195	8,282
PAT	145	2,437	765
Total Assets	1,88,259*	2,38,520*	2,48,950#
Net NPA (%)	1.53	0.86	0.70
ROTA (%)	0.08	1.14	1.26^

A: Audited UA: Unaudited; Note: 'the above results are latest financial results available' ^annualized

*Adjusted for net of intangibles, deferred tax asset.
#Not adjusted for net of intangibles, deferred tax asset.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

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

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

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Long-term bank facilities*	-	-	-	-	692.38	CARE AA+; Stable
Non-convertible debentures	INE688I08012	28-02-2013	10.3	28-02-2023	0	Withdrawn
Non-convertible debentures	INE688I08020	28-02-2013	10.3	28-02-2023	0	Withdrawn
Non-convertible debentures	INE688I08038	08-03-2013	11	08-03-2099	0	Withdrawn
Non-convertible debentures	INE688I08046	14-03-2013	11	14-03-2099	0	Withdrawn
Non-convertible debentures	INE688I08053	17-05-2013	9.5	17-05-2028	49.5	CARE AA+; Stable
Non-convertible debentures	INE688I08061	24-05-2013	10.65	24-05-2099	0	Withdrawn
Non-convertible debentures	INE688I08079	23-09-2014	10.5	23-09-2099	49.6	CARE AA+; Stable
Non-convertible debentures	INE688I08087	29-09-2015	9.4	29-09-2025	49.3	CARE AA+; Stable
Non-convertible debentures	INE688I08095	30-10-2015	9.25	30-10-2025	74.6	CARE AA+; Stable
Non-convertible debentures	INE688I08103	20-11-2015	9.25	20-11-2025	25	CARE AA+; Stable
Non-convertible debentures	INE688I08111	15-12-2015	9.25	15-12-2025	25	CARE AA+; Stable

Non-convertible debentures	INE688I08129	29-12-2015	9.25	29-12-2025	34.2	CARE AA+; Stable
Non-convertible debentures	INE688I08145	01-03-2016	10.5	01-03-2099	56.8	CARE AA+; Stable
Non-convertible debentures	INE092T08DB6	31-05-2016	9.1	31-05-2023	0	Withdrawn
Non-convertible debentures	INE688I08152	06-06-2016	9.75	06-06-2099	28.2	CARE AA+; Stable
Non-convertible debentures	INE092T08DD2	13-06-2016	9.1	13-06-2023	0	Withdrawn
Non-convertible debentures	INE092T08DG5	19-07-2016	9.15	19-07-2023	0	Withdrawn
Non-convertible debentures	INE688I08160	25-07-2016	9.24	24-07-2026	30	CARE AA+; Stable
Non-convertible debentures	INE092T08DM3	20-09-2016	8.75	18-09-2026	25	CARE AA+; Stable
Non-convertible debentures	INE092T08EC2	03-05-2017	8.45	03-05-2024	70	CARE AA+; Stable
Non-convertible debentures	INE688I08178	24-08-2017	8.25	24-08-2027	146.2	CARE AA+; Stable
Non-convertible debentures	INE688I08186	18-09-2017	8.6	18-09-2099	72.5	CARE AA+; Stable
Non-convertible debentures	INE092T08EU4	29-09-2017	8.25	29-09-2022	0	Withdrawn
Non-convertible debentures	INE092T08EN9	08-12-2017	8.25	08-12-2022	0	Withdrawn
Non-convertible debentures	INE092T08ES8	04-05-2018	8.24	15-05-2023	0	Withdrawn
Non-convertible debentures	INE688I08194	07-06-2018	9.1	07-06-2024	29	CARE AA+; Stable
Non-convertible debentures	INE688I08202	07-06-2018	9.1	06-06-2025	68	CARE AA+; Stable
Non-convertible debentures	INE092T08EW0	12-12-2018	8.6	12-12-2022	0	Withdrawn
Non-convertible debentures	INE092T08EX8	12-12-2018	8.69	12-12-2023	349.4	CARE AA+; Stable

*Bank facilities are closed/repaid but not withdrawn

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Borrowings-Secured Long Term Borrowings	LT	1874.68	CARE AA+; Stable	-	1)CARE AA; Stable (04-Oct-22)	1)CARE AA; Stable (07-Jan-22) 2)CARE AA; Stable (06-Oct-21)	1)CARE AA; Stable (08-Oct-20)
2	Short Term Instruments-Short Term Borrowing	ST	-	-	-	-	-	1)Withdrawn (30-Oct-20)

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities- Not applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Non-convertible debenture	Simple
2	Long term bank facilities	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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