CRISIL Ratings

Rating Rationale

June 27, 2024 | Mumbai

Indian Overseas Bank

Long term ratings upgraded to 'CRISIL AA+/Stable/CRISIL AA/Stable'; Certificate of Deposits Withdrawn

Rating Action

Rs.200000 Crore Fixed Deposits	**CRISIL AA+/Stable (Upgraded from 'CRISIL AA/Positive'; Rating on Notice of Withdrawal)**
Rs.500 Crore Tier II Bonds (Under Basel III)	**CRISIL AA/Stable (Upgraded from 'CRISIL AA-/Positive')**
Rs.300 Crore Tier II Bonds (Under Basel III)	**Withdrawn (CRISIL AA-/Positive)**
Certificate of Deposits	**Withdrawn (CRISIL A1+)**

Note: None of the Directors on CRISIL Ratings Limited's Board are members of rating committee and thus do not participate in discussion or assignment of any ratings. The Board of Directors also does not discuss any ratings at its meetings.
1 crore = 10 million
Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has upgraded the long-term ratings on the tier-II bonds (under Basel III) and fixed deposit programme of Indian Overseas Bank (IOB) to **'CRISIL AA+/CRISIL AA'** from 'CRISIL AA/CRISIL AA- while revising the outlook to '**Stable**' from 'Positive'.

Also, CRISIL Ratings has **withdrawn** its short-term ratings on certificate of deposits and long term rating on tier-II bonds of Rs 300 crore as the outstanding against the same is nil and on receipt of confirmation from the debenture trustee (see Annexure - Details of Rating Withdrawn for details). Ratings on Fixed Deposits have been placed on **notice for withdrawal**. The withdrawals are in line with the CRISIL Ratings withdrawal policy.

The rating action factors in sustained improvement in earnings and asset quality, and strengthening of capital position, which is likely to be maintained over the medium term. The bank has been profitable since the past four fiscals (fiscal 2021) owing to lower credit cost backed by less incremental stress as well as improving net interest margins (NIMs). Supported by regular capital infusion, the bank was able to build sufficient buffer for its non-performing assets (NPAs) with a provision coverage ratio (PCR)[1] of 82% as on March 31, 2024. With higher provisions and lower slippages, the bank is expected to maintain profitability over the medium term.

Asset quality, while moderate, has seen sequential improvement with gross NPA reduced to 3.1% as on March 31, 2024, compared with 7.4% a year earlier. This improvement was mainly driven by higher write-offs as well as controlled slippages.

Besides, the capital position has improved, supported by timely capital infusion and internal accruals, leading to tier 1 and overall capital adequacy ratio (CAR) improving to 14.5%, and 17.3% respectively, as on March 31, 2024, from 12.9% and 16.1%, a year earlier.

Capital position is supported by regular fund infusion and expectation of strong support from the majority stakeholder, the government of India (GoI). In March 2021, GoI infused Rs 4,100 crore (Rs 8,217 crore in fiscal 2020; Rs 5,963 crore in fiscal 2019 and Rs 5,794 crore in fiscal 2018).

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[1] PCR including technical write-off was 97% as on March 31, 2024.

Analytical Approach

CRISIL Ratings has considered the standalone business and financial risk profiles of IOB and has factored in the strong support that the bank is expected to receive from its majority owner, GoI, both on an ongoing basis and in the event of distress.

Key Rating Drivers & Detailed Description

Strengths:

Strong support from the majority owner, GoI

The ratings continue to factor in the expected strong government support both on an ongoing basis and in the event of distress. This is because GoI is both the majority shareholder in public sector banks (PSBs) and the guardian of India's financial system. Stability of the banking sector is of prime importance to the government given its criticality to the economy, strong public perception of sovereign backing for PSBs and severe implications of any PSB failure, in terms of political fallout, systemic stability and investor confidence. The majority ownership creates a moral obligation on GoI to support PSBs, including IOB.

As part of the Indradhanush framework, the government had pledged to infuse at least Rs 70,000 crore in PSBs over fiscals 2015-2019, of which Rs 25,000 crore per annum was infused in fiscals 2016 and 2017. In October 2017, the government outlined a recapitalisation package of Rs 2.11 lakh crore over fiscals 2018-2019. IOB received Rs 5,794 crore in fiscal 2018 and Rs 5,963 crore in fiscal 2019 under this package. Also, GoI allocated Rs 70,000 crore in fiscal 2020, of which IOB received Rs 8,217 crore. During fiscal 2021, GoI infused Rs 4,100 crore. Thus, over fiscals 2018-2021, GoI infused Rs 22,974 crore into IOB. This has helped the bank to improve its capital ratios and meet regulatory requirements. As on March 31, 2024, Tier 1 and overall CAR stood at 14.5% and 17.3%, respectively.

Adequate capital position supported by internal accrual will limit the bank’s dependence on further capital support from GoI.

Weakness:
Moderate asset quality and earnings profile, albeit improving
Asset quality remains moderate, albeit improving, with NPA ratios comparable with the industry average. Gross NPAs improved to 3.1% as on March 31, 2024, from 7.4% as on March 31, 2023 (9.8% as on March 31, 2022, 11.7% as on March 31, 2021; 14.8% as on March 31, 2020), aided by write-offs and controlled slippages. The bank has written off a cumulative Rs 43,104 crore over fiscals 2019-2024, of which Rs 7,214 crore was written off during fiscal 2024 (Rs 3,413 crore in fiscal 2023, Rs 3,769 crore in fiscal 2022, Rs 4,618 crore in fiscal 2021, Rs 16,407 crore in fiscal 2020 and Rs 7,683 crore in fiscal 2019). Aside from write offs, structural improvement in asset quality is also seen through lower slippages (as a percentage of net opening advances) which were down to 0.9% in fiscal 2024 from 3.1% in fiscal 2023 and 4.0% in fiscal 2022; after remaining elevated in prior years (5.4% in fiscal 2020, 6.7% in fiscal 2019 and 12.0% in fiscal 2018).

Earnings, while modest, have been improving with profit reported since the past three fiscals. The bank reported net profit in fiscal 2021 after six consecutive years of incurring losses. Operating margin improved owing to continual reduction in credit cost to 1.0% in fiscal 2024, 1.2% in fiscal 2023 and 1.4% in fiscal 2022 from 1.9% in fiscal 2021 and 4.7% in fiscal 2020. Profit after tax (PAT) stood at Rs 2,656 crore in fiscal 2024 with return on assets (ROA) of 0.8% backed by improved NIM and controlled credit cost. Ability to sustain improvement in profitability will remain a key monitorable, with expected impact on NIMs from higher funding cost and trend in slippages determining the trajectory of credit cost.

Liquidity: : Strong
Liquidity is supported by a sizeable retail deposit base, forming a large chunk of total deposits. Liquidity coverage ratio was 139% as on March 31, 2024, which is higher than the regulatory requirement. Also, the bank benefits from access to systemic sources of funds such as the liquidity adjustment facility from the RBI, call money market and refinance limits from sources such as National Housing Bank and National Bank for Agriculture and Rural Development.

ESG profile
CRISIL Ratings believes the environment, social and governance (ESG) profile of Indian Overseas Bank supports its already strong credit risk profile.

The ESG profile for financial sector entities factors in governance as a key differentiator. The sector has a reasonable social impact because of its substantial employee and customer base and can play a key role in promoting financial inclusion. While the sector does not have direct adverse environmental impact, lending decisions may have a bearing on the environment.

IOB has an ongoing focus on strengthening the various aspects of its ESG profile.

Key ESG highlights:

- ESG disclosures of the bank are evolving, and it is in the process of strengthening the disclosures
- IOB’s scope 1 and 2 emissions intensity has reduced by ~50% y-o-y in fiscal 2024
- The bank has introduced a green deposit scheme under which deposits raised shall be utilized for financing green activities and projects.
- The bank’s total workforce comprised around 36% women as on March 31, 2024, and it has taken initiatives to promote gender equality within the organisation.
- The governance structure is characterized by 50% of independent directors with chairman also being independent director, 100% investor complaint redressal rate and extensive financial disclosures.

There is growing importance of ESG among investors and lenders. The commitment of IOB to ESG will play a key role in enhancing stakeholder confidence, given its access to domestic and foreign capital markets.

Outlook Stable
CRISIL Ratings believes IOB will continue to benefit from government support on an ongoing basis as well as in the event of distress. Asset quality and profitability are expected to maintain positive trajectory, however, will remain a monitorable

Rating Sensitivity factors
Upward factors

- Significant improvement in overall market position over the medium term
- Sustained improvement in profitability, with ROA over 1.0% on steady-state basis

Downward factors

- Material change in shareholding or expectation of support from the government

- Decline in CAR below minimum regulatory requirements (including CCB, which is Tier I of 9.5% and overall, CAR of 11.5%)

About the Bank

Set up in 1937 by Mr M Ct M Chidambaram Chettyar, IOB was nationalised in 1969. Headquartered in Chennai, the bank had 3,236 domestic branches, 4 overseas branches and 3,506 automated teller machines as on March 31, 2024. As on March 31, 2024, total advances and deposits were Rs 219,018 crore and Rs 285,905 crore, respectively. The loan portfolio comprises corporate loans (25%), MSME loans (19%), agriculture loans (25%), retail loans (22%) and overseas loans (8%). Current account and savings account (CASA) deposits to total deposits ratio was 43.9% as on March 31, 2024 (43.7% as on March 31, 2023, and 43.4% as on March 31, 2022).

For fiscal 2024, the bank reported PAT of Rs 2,656 crore on total income (net of interest expense) of Rs 15,486 crore, compared with Rs 2,099 crore and Rs 12,364 crore, respectively, in fiscal 2023.

Key Financial Indicators

As on / for the half year ended March 31		2024	2023
Total assets	Rs crore	352,034	313,746
Total income (net of interest expense)	Rs crore	15,486	12,364
PAT	Rs crore	2,656	2,099
Gross NPA	%	3.1	7.4
Overall CAR	%	17.3	16.1
Return on assets	%	0.8	0.7

Any other information:

Note on tier-II instruments (under Basel III)

The distinguishing feature of tier-II capital instruments under Basel III is the existence of the point of non-viability (PONV) trigger, the occurrence of which may result in loss of principal to the investors and hence, to default on the instrument by the issuer. According to the Basel III guidelines, the PONV trigger will be determined by the RBI. CRISIL Ratings believes the PONV trigger is a remote possibility in the Indian context, given the robust regulatory and supervisory framework and the systemic importance of the banking sector. The inherent risk associated with the PONV feature is adequately factored into the rating on the instrument.

Note on complexity levels of the rated instrument:

CRISIL Ratings` complexity levels are assigned to various types of financial instruments and are included (where applicable) in the 'Annexure - Details of Instrument' in this Rating Rationale.

CRISIL Ratings will disclose complexity level for all securities - including those that are yet to be placed - based on available information. The complexity level for instruments may be updated, where required, in the rating rationale published subsequent to the issuance of the instrument when details on such features are available.

For more details on the CRISIL Ratings` complexity levels please visit www.crisilratings.com. Users may also call the Customer Service Helpdesk with queries on specific instruments.

Annexure - Details of Instrument(s)

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs crore)	Complexity level	CRISIL rating with outlook
INE565A08035	Tier II bonds	24-Sep-2019	9.0802	24-Sep-2029	500	Simple	CRISIL AA/Stable
NA	FD programme	NA	NA	NA	200000	Simple	CRISIL AA+/Stable (Notice of Withdrawal)

Annexure - Details of Rating Withdrawn

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs crore)	Complexity level	Rating
INE565A09264	Tier II bonds	10-Dec-2018	11.7	10-Dec-2028	300	Simple	Withdrawn
NA	Certificate of deposits programme	NA	NA	7-365 days	NA	Simple	Withdrawn

Annexure - Rating History for last 3 Years

	Current			2024 (History)		2023		2022		2021		Start of 2021
Instrument	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Certificate of Deposits	ST	0.0	Withdrawn		--	28-06-23	CRISIL A1+	29-06-22	CRISIL A1+	24-12-21	CRISIL A1+	CRISIL A1+
			--		--		--		--	31-07-21	CRISIL A1+	--
Fixed Deposits	LT	200000.0	CRISIL AA+/Stable		--	28-06-23	CRISIL AA/Positive	29-06-22	CRISIL AA/Stable	24-12-21	F AA/Positive	F AA/Stable

			--		--		--		--	31-07-21	F AA/Stable	--
Lower Tier-II Bonds (under Basel II)	LT		--		--		--		--	31-07-21	Withdrawn	CRISIL A+/Stable
Perpetual Tier-I Bonds (under Basel II)	LT		--		--		--		--		--	Withdrawn
Tier II Bonds (Under Basel III)	LT	500.0	CRISIL AA/Stable		--	28-06-23	CRISIL AA-/Positive	29-06-22	CRISIL AA-/Stable	24-12-21	CRISIL A+/Positive	CRISIL A+/Stable
			--		--		--		--	31-07-21	CRISIL A+/Stable	--
Upper Tier-II Bonds (under Basel II)	LT		--		--		--		--	31-07-21	Withdrawn	CRISIL A-/Stable

All amounts are in Rs.Cr.

Criteria Details

Links to related criteria
Rating Criteria for Banks and Financial Institutions
CRISILs criteria for rating fixed deposit programmes
CRISILs Criteria for rating short term debt
Rating criteria for Basel III - compliant non-equity capital instruments
Criteria for Notching up Stand Alone Ratings of Entities Based on Government Support

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