July 20, 2023

SBM Bank (India) Ltd: Ratings reaffirmed; Outlook revised to Negative from Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Basel III Tier II Bond Programme	250.00	250.00	[ICRA]A+ (Negative); Reaffirmed and outlook revised to Negative from Stable
Certificates of Deposit	500.00	500.00	[ICRA]A1+; Reaffirmed
Total	**750.00**	**750.00**	

**Instrument details are provided in Annexure I*

Rationale

The revision in the outlook on the long-term rating of SBM Bank (India) Ltd factors in its weakened profitability levels due to higher pressure on fee income, which is likely to continue in the near term. This follows the regulatory actions in recent months, including restrictions on the Liberalised Remittance Scheme (LRS), actions/observations linked to businesses with fintech partnerships/segments, provisioning on remaining collections from tax collected at source (TCS) on the LRS and provisioning linked to operating income as instructed by the regulator. As the bank scaled up its businesses in the above-mentioned segments, resulting in elevated operating expenditure, the decline in revenue from these segments has adversely impacted its operating leverage. The bank is currently engaged with the regulator and is addressing these observations. The timely resolution of the same could enable it to scale back in some of these segments over time, though this remains to be seen.

Amid these developments, SBM Bank (India) Ltd's total deposit base also declined, although this has largely stabilised now, and its overall liquidity levels remain adequate. Moreover, the current account deposit base has declined as some of the growth in the last two years was driven by the growth in the fintech/credit card partnerships, which is now likely to decline. The changing deposit mix and lower deposit base are also expected to weigh on the profitability levels. As the bank shifts away from these segments, the overall loan book growth as well as non-interest/fee income levels are likely to moderate and its ability to revive fee income or control operating expenses will remain critical for improving profitability. Amid all this, the asset quality levels have largely remained comfortable, although the suboptimal operating profitability continues to restrict the bank's ability to absorb an increase in the credit costs if the asset quality weakens.

Additionally, the capital cushions over the regulatory requirements have continued to narrow despite periodic support from the parent. This is due to the growth as well as the increase in the risk-weighted density of the book on account of the regulatory changes. This is unlikely to improve materially unless supported by a capital raise or infusion from the parent. With declining capital cushions and muted internal capital generation, the bank's dependence on fresh capital raises will remain high over the near to medium term. Furthermore, clarity on any relief/easing of restrictions or penalties imposed on the bank will remain a monitorable.

The ratings continue to factor in the parentage in the form of SBM Holdings Limited, the ultimate holding company of SBM Bank (Mauritius) Limited (rated Baa3 (stable)/P-3/BCA ba1 by Moody's) and SBM Bank (India) Ltd. SBM Holdings Limited is the holding company of all the banking and financial activities of the SBM Group (Mauritius). It houses two intermediate investment arms of the Group, namely SBM (Bank) Holdings Limited for banks and SBM (NFC) Holdings Limited for non-banks, which together operate banking and non-banking entities across Africa and India. Furthermore, the Government of Mauritius (rated Baa2 (negative) by Moody's) is the largest shareholder in SBM Holdings Limited. ICRA will continue to closely monitor

the credit profile and the impact of international developments on both SBM Holdings Limited and SBM Bank (Mauritius) Limited as these could also be the rating drivers of SBM Bank (India) Ltd in the near to medium term.
Over and above the requirement of meeting the capitalisation metrics, i.e. CET-I, Tier-I and CRAR above 8.0%, 9.5% and 11.5%, respectively, the bank is required to maintain a minimum net worth of Rs. 500 crore. This is as per the Reserve Bank of India's (RBI) framework for the wholly-owned subsidiaries (WOS) of foreign banks in India. SBM (Bank) Holdings Limited has undertaken to provide necessary financial support to SBM Bank (India) Ltd if it is unable to meet any of its liabilities and will also ensure that it maintains a minimum net worth of Rs. 500 crore. The parent infused Rs. 100 crore of equity into SBM Bank (India) Ltd in FY2022, which led to further expansion in the overall net worth position over the regulatory levels. ICRA expects the parent to continue supporting the bank in meeting the capital requirements, if any.

Key rating drivers and their description

Credit strengths

Part of SBM Group (Mauritius) – ICRA continues to factor in the parentage of SBM Bank (India) Ltd and its position as a step-down WOS of SBM Holdings Limited, the ultimate holding company of SBM Bank (Mauritius) Limited. SBM Holdings Limited's shareholders include the Government of Mauritius, which, along with other state-owned entities including state-owned pension funds, remains the largest shareholder with a 42% stake. Additionally, SBM Bank (Mauritius) Limited is the second largest bank in Mauritius with assets of $6.08 billion as on December 31, 2022. SBM Holdings Limited's operations are spread across countries like Kenya and Madagascar. The parent company's continued strong commitment towards supporting the Indian operations serves as a credit positive. Strong operational linkages with the Group in terms of ownership, a shared name and its overall importance in advancing the Group's growth plans in the region provide further comfort.

The parent has demonstrated support through capital infusions in the past as the Indian branches transitioned to the subsidiary model with SBM (Bank) Holdings Limited infusing capital of ~Rs. 200 crore during FY2019-FY2022. This helped the overall growth momentum during the year. ICRA factors in the strong likelihood of continued support from the parent to the Indian entity, if required. Moreover, SBM Bank (Holdings) Limited has given in-principle approval to provide necessary financial support to the Indian entity to meet any liability that the bank is unable to meet. This remains in line with the RBI's framework for the WOS of foreign banks in India.

Comfortable asset quality metrics – The fresh non-performing advances (NPA) generation rate remained at a manageable level of 0.83% in FY2023 (1.01% in FY2022). This, along with the rapid scaling up of the book, supported the headline asset quality levels with the gross NPA (GNPA) and net NPA (NNPA) at 1.98% and 0.34%, respectively, as on March 31, 2023 (2.10% and 0.39%, respectively, as on March 31, 2022) while the provision coverage ratio (PCR), excluding write-offs, was satisfactory at 82.98% as on March 31, 2023 (81.62% as on March 31, 2022). Furthermore, the overall monitorable book of the bank, comprising the overdue (special mention account (SMA) 1 and SMA 2) and restructured book, remained manageable at 0.30% of standard advances as on March 31, 2023.

The loan book concentration remains high with the top 20 exposures accounting for 16.09% of the total exposures and 167.51% of the bank's net worth as on March 31, 2023 although it has come down from 20.02% and 170.29%, respectively, as on March 31, 2022. Given the weak operating profitability and the concentrated loan book, any slippage from the corporate borrowers could drive an increase in the credit provisions, putting pressure on the bank's profitability and capital position.

Credit challenges

Operating profitability and return metrics expected to remain modest – Despite the relative improvement in the net interest margin (NIM) to 2.33% of the average total assets (ATA) in FY2023 (1.95% in FY2022) as well as the expansion of retail products (co-branded credit cards, etc), forex income, etc, which supported the traction in non-interest income, the operating cost remained elevated at 4.13% of average assets (2.90% in FY2022). This led to a muted core operating profitability of 0.34% of

ATA in FY2023 (0.72% in FY2022). However, as fresh gross slippages in FY2023 and FY2022 largely remained in check and given the relatively high provision coverage on the legacy NPAs, total provisions including credit costs remained low at 0.19% of ATA in FY2023 (0.55% in FY2022). Despite this, the return indicators remained suboptimal with the return on assets (RoA) at 0.23% in FY2023 (0.25% in FY2022).

The recent observations and regulatory tightening around some of the business segments that were being pursued actively by the bank (including credit cards/secured cards in partnerships with various fintech companies) are expected to drive down fee income from these segments, which had seen meaningful traction in recent years. As SBM Bank (India) Ltd is now gradually shifting away from these businesses, non-interest income could decline. Hence, its ability to curtail its operating expenditure will be critical to drive an improvement in its profitability. Furthermore, the restriction on the handling of LRS transactions on behalf of its customers is expected to curtail fee income from this business. Besides this, the bank has reported non-recovery of TCS from customers relating to debit card LRS transactions, which could result in provisions on the amount not recovered from such customers in FY2024 as well. Additionally, the bank has been directed to create provisions linked to its operating income {due to delay in implementation of Income Recognition and Asset Classification (IRAC) norms on NPA automation}, which could put pressure on its profitability. However, the bank is in the process of recovering the TCS from these customers as well as addressing the aforementioned observations. The timely resolution of these could enable the bank to release some of these provisions, which remains to be seen. Furthermore, the changing deposit mix could limit the bank's ability to bring down its cost of funds meaningfully in the near to medium term. Collectively, these factors are expected to keep SBM Bank (India) Ltd's overall profitability muted over the near to medium term.

Loss-absorption cushions narrow – The bank's overall risk-weighted density increased in FY2023 due to the higher risk-weighting of some of the segments in which it had operations. This was also driven by the regulatory changes related to these segments. This, along with muted profitability levels and the increase in the loan book, drove down the Tier I ratio to 11.46% as on March 31, 2023 (16.06% as on March 31, 2022). As a result, SBM Bank (India) Ltd's loss-absorption cushions have continued to decline, which would also limit its near-term growth prospects. While the parent has periodically infused capital into the bank, helping shore up its capital position and supporting growth, its near-to-medium-term dependency on fresh capital raises or parent support is likely to continue.

SBM Bank (India) Ltd's overall net worth increased to Rs. 740 crore as on March 31, 2023 from Rs. 715 crore as on March 31, 2022, and remains above the regulatory requirement of Rs. 500 crore for the WOS of foreign banks. This was mainly attributable to the Rs. 100-crore infusion by the parent in FY2022, as internal capital generation remained suboptimal. Further, as the bank will continue to push towards growing its franchise, the cost-to income level is likely to remain elevated over the near to medium term, resulting in modest internal capital generation.

Deposit growth remains sluggish amid tightening regulations – SBM Bank (India) Ltd's deposit growth slowed to ~8% in FY2023 (Rs. 7,319 crore as on March 31, 2023) compared to the much stronger year-on-year (YoY) growth of ~76% in FY2022. Net advances growth slowed down correspondingly to ~11% in FY2023 (Rs. 4,836 crore as on March 31, 2023) from ~49% in FY2022, albeit on a low base. The deceleration in the growth momentum was largely due to the uncertainty and regulatory actions on the bank in January 2023, following which its deposit base as well as loan book declined. These developments, along with the gradual shift from fintech segments, impacted deposit traction and slowed down the growth in advances. As some of the business/fintech arrangements helped shore up the bank's current account level, the gradual shift from this has also led to a decline in its low-cost current account deposit level (declined to Rs. 1,114 crore as on March 31, 2023 from Rs. 1,426 crore as on March 31, 2022). This will add pressure to the cost of funds.

Furthermore, the overall deposit concentration level, as reflected by the share of the top 20 depositors, remained high at 22% of the total deposits as on March 31, 2023 (34% as on March 31, 2022 and 38% as on March 31, 2021) although it is comparatively below past levels. Going forward, SBM Bank (India) Ltd's ability to grow its franchise will drive its ability to build up a granular low-cost deposit base.

Liquidity position: Adequate

Following the LRS restrictions imposed by the RBI in January 2023, the bank's overall deposit base declined to some extent before stabilising in the following weeks. It maintained its statutory liquidity ratio (SLR) at ~31-41% of net demand and time liabilities (NDTL) on the fortnightly reporting dates between January 2023 and May 2023, which was ~13-23% above the regulatory minimum of 18%. As a result, the bank's daily average liquidity coverage ratio stood at 144% in Q4 FY2023, well above the regulatory requirement of 100%. Despite the high level of surplus Government securities, which can be sold to generate liquidity, SBM (Bank) India Ltd has negative cumulative mismatches in the less than 1-year bucket because of the relatively longer tenor of its loans in relation to deposits as per the structural liquidity statement (SLS). Going forward, its ability to maintain a high rollover rate of deposits and improve the granularity of its deposit base will remain a key factor for sustaining liquidity.

Rating sensitivities

Positive factors – ICRA could revise the outlook to Stable if there is a sustained improvement in the profitability levels or in the capital cushions. An improvement in the credit profile of the SBM Group (Mauritius) will also be a positive factor.

Negative factors – ICRA could downgrade the ratings if the Tier I capital cushion remains below 2% over the regulatory level (9.5%) and the earnings profile stays weak on a sustained basis. Further, a deterioration in the credit profile of the SBM Group (Mauritius) or lack of adequate funding support to maintain its capital and liquidity cushions, if required, will be negative triggers.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA Rating Methodology for Banks and Financial Institutions Impact of Parent or Group Support on Issuer Credit Rating
Parent/Group support	**Group Company: SBM Holdings Limited** ICRA expects SBM Bank (India) Ltd's parent, SBM Holdings Limited, which is also the holding company of SBM Bank (Mauritius) Limited, to be willing to extend financial support to the bank, if required, given the high strategic importance it holds for SBM Holdings Limited for meeting its diversification objectives and for driving growth in the region. SBM Holdings Limited and SBM Bank (India) Ltd share a common name, which, in ICRA's opinion, would persuade SBM Holdings Limited to provide financial support to the bank to protect its reputation from the consequences of a group entity's distress.
Consolidation/Standalone	Standalone

About the company

The SBM Group (Mauritius) commenced banking operations in India in 1994 with four branches in Mumbai, Chennai, Hyderabad and Ramachandrapuram, which operated as branches of SBM Bank (Mauritius) Limited. In December 2018, the RBI sanctioned a Scheme of Amalgamation of the Indian branches of SBM Bank (Mauritius) Limited and SBM Bank (India) Ltd, which was granted a licence to carry out banking operations under the WOS mode. The scheme became effective from December 1, 2018. Following this, all the Indian branches started functioning as branches of SBM Bank (India) Ltd. As on June 30, 2021, the bank had eight branches in India against four at the time of its conversion to a WOS.

The bank reported a net profit of Rs. 21 crore in FY2023 on a total asset base of Rs. 10,125 crore as on March 31, 2023. The CRAR stood at 16.16% as on March 31, 2023 (17.28% as on March 31, 2022). The asset quality improved marginally with the GNPA and NNPA at 1.98% and 0.34%, respectively, as on March 31, 2023 (2.10% and 0.39%, respectively, as on March 31, 2022).

SBM Bank (Mauritius) Limited

Established in 1973, it is the second-largest domestic bank in Mauritius. It provides retail, corporate, small and medium-sized enterprise and cross-border banking as well as other services, including bancassurance, financial market services such as structured treasury and money market instruments, and custodial services. In 2014, the Group restructured its operations and segregated its banking operations from its non-banking operations. SBM Holdings Limited was established as the new holding company for the operating companies and is the entity listed on the Stock Exchange of Mauritius.

For calendar year (CY) 2022, SBM Bank (Mauritius) Limited reported a net profit of $79.9 million on total assets of $6.08 billion as on December 31, 2022 compared to a net profit of $50.1 million in CY2021 on total assets of $6.26 billion as on December 31, 2021. It reported a Tier I capital of 15.32% as on December 31, 2022 compared to 17.33% as on December 31, 2021.

SBM Holdings Limited

SBM Holdings Limited is the ultimate holding company of SBM Bank (India) Ltd and SBM Bank (Mauritius) Limited. On a consolidated basis, it reported a net profit of $82.32 million on total assets of $8.18 billion as on December 31, 2022 compared to a net profit of $41.60 million in CY2021 on total assets of $8.12 billion as on December 31, 2021.

Key financial indicators (standalone)

SBM Bank (India) Ltd	FY2021	FY2022	FY2023
Net interest income	78	125	212
Operating profit (excl. trading gains)	24	46	31
Profit after tax	19	16	21
Loan book	2,917	4,354	4,836
Total assets	4,739	8,085	10,125
Net interest margin / Average total assets	2.17%	1.95%	2.33%
Return on average assets	0.52%	0.25%	0.23%
Return on net worth	3.11%	2.28%	2.83%
Tier I	19.46%	16.06%	11.46%
CRAR	20.72%	17.28%	16.16%
Gross NPA	2.97%	2.10%	1.98%
Net NPA	0.90%	0.39%	0.34%
PCR (excl. TWO)	70.33%	81.62%	82.98%
Solvency (Net NPA/Tier I capital)	5.09%	2.55%	2.41%

Source: SBM Bank (India) Ltd & ICRA Research; Amount in Rs. crore
All ratios as per ICRA's calculations

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022		Date & Rating in FY2021
					Jul-20-2023	Jul-28-2022	Sep-17-2021	Jun-03-2021	May-26-2020
1	**Basel III Tier II Bonds**	Long term	250	224	**[ICRA]A+ (Negative)**	**[ICRA]A+ (Stable)**	**[ICRA]A+ (Stable)**	-	-
2	**Certificates of Deposit Programme**	Short term	500	220	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**

Source: ICRA Research

Complexity level of the rated instrument

Instrument	Complexity Indicator
Basel III Tier II Bonds	Highly Complex
Certificates of Deposit	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instruments credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE07PX16376	**Certificates of Deposit**	Jun-19-2023	7.90%	Dec-21-2023	80.00	[ICRA]A1+
INE07PX16368	**Certificates of Deposit**	Jun-19-2023	7.90%	Dec-27-2023	75.00	[ICRA]A1+
INE07PX16350	**Certificates of Deposit**	Jun-16-2023	7.90%	Dec-22-2023	65.00	[ICRA]A1+
NA	**Certificates of Deposit**	Yet to be placed	NA	7-365 days	280.00	[ICRA]A1+
INE07PX08019	**Basel III Tier II Bonds**	Apr-05-2022	9.75%	Apr-05-2032^	125.00	[ICRA]A+ (Negative)
INE07PX08027	**Basel III Tier II Bonds**	Jan-24-2023	9.88%	Jan-24-2033*	99.00	[ICRA]A+ (Negative)
NA	**Basel III Tier II Bonds**	Yet to be placed	NA	-	26.00	[ICRA]A+ (Negative)

** As on July 19, 2023; ^Call option available on April 5, 2027; *Call option available on January 24, 2028*

Source: SBM Bank (India) Ltd

Annexure II: List of entities considered for consolidated analysis – Not applicable

ANALYST CONTACTS

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

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

Gayatri Kulkarni
+91 22 6114 3471
gayatri.kulkarni@icraindia.com

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

Devesh Lakhotia
+91 22 6114 3404
devesh.lakhotia@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

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents.