Ratings

CRISIL
An S&P Global Company

Rating Rationale

December 17, 2019 | Mumbai

Allahabad Bank

'CRISIL AA-' assigned to Tier II Bonds (Under Basel III); Ratings placed on 'Watch Positive'

Rating Action

Rs.1500 Crore Tier II Bonds (Under Basel III)	**CRISIL AA- (Assigned; Placed on 'Rating Watch with Positive Implications')**
Rs.500 Crore Tier II Bonds (Under Basel III)	**CRISIL AA- (Placed on 'Rating Watch with Positive Implications')**
Rs.1000 Crore Tier II Bonds (Under Basel III)	**CRISIL AA- (Placed on 'Rating Watch with Positive Implications')**
Lower Tier II Bonds (Under Basel II) Aggregating Rs.850 Crore	**CRISIL AA- (Placed on 'Rating Watch with Positive Implications')**
Upper Tier II Bonds (Under Basel II) Aggregating Rs.1000 Crore	**CRISIL A+ (Placed on 'Rating Watch with Positive Implications')**
Tier I Perpetual Bonds (Under Basel II) Aggregating Rs.300 Crore	**CRISIL A+ (Placed on 'Rating Watch with Positive Implications')**

1 crore = 10 million
Refer to annexure for Details of Instruments & Bank Facilities

Detailed Rationale
CRISIL has assigned its **'CRISIL AA-'** rating to Rs.1500 Crore Tier II Bonds (Under Basel III) of Allahabad Bank while placing its ratings on **'Rating Watch with Positive Implications'**.

CRISIL has also withdrawn its rating on Lower Tier-II Bonds (under Basel II) of Rs. 850 crore, Perpetual Tier-I Bonds (under Basel II) of Rs. 150 crore and Upper Tier-II Bonds (under Basel II) of Rs. 500 crore (See Annexure 'Details of Rating Withdrawn' for details) in line with its withdrawal policy.

On August 30, 2019, Ministry of Finance announced a set of reforms for public sector banks (PSBs) including consolidation, capital infusion and measures to enhance governance standards. A key announcement was also the amalgamation of 6 PSBs into 4 anchor PSBs. As part of this announcement, it was proposed to amalgamate Allahabad Bank with Indian Bank. In response to the announcement, CRISIL had published a Credit Bulletin on September 5, 2019 conveying that it will continue to closely monitor developments and engage with various stakeholders, and take appropriate rating action thereafter.

The ratings on the debt instruments of Allahabad Bank has now been placed on 'Watch with Positive Implications' given the significant progress on the amalgamation including approvals from the Boards of Directors of both banks. CRISIL expects that the credit profile of the merged entity to be better than that of Allahabad Bank currently. On September 16, 2019, in-principle approval from the Board of Directors of Allahabad Bank was received. Later, on November 19, 2019, Alternative Mechanism also accorded its in-principle approval for the amalgamation of Allahabad Bank with Indian Bank. Further, CRISIL has had discussions with several of the amalgamating banks and understands that the joint consultation process in terms of branch rationalization, alignment of policies, processes and products, joint training of staff, etc. is already underway. The merger is expected to be completed after receipt of all regulatory approvals. CRISIL will resolve the rating watch once clarity emerges on the merger completion. On resolution of the rating watch, the rating on the new instrument is unlikely to move by more than one rating category.

In terms of pro-forma merged financials, the merged bank would have total assets of Rs 5.4 lakh crore, with gross non-performing assets (NPAs) of 12.7% as on September 30, 2019. Common equity tier I (CET-I), Tier I and overall capital adequacy ratio (CAR) of the merged entity were at 10.5%, 10.7% and 12.9% as on September 30, 2019. On the business side, there are potential synergies stemming from a larger distribution network with deeper penetration in key states and operational efficiencies. The branch network strength of Indian Bank and Allahabad Bank will complement each other and the merged bank will have significant presence in the North, East and South of the country.

Till the amalgamation is completed, the ratings on the debt instruments of Allahabad Bank will continue to factor in the expectation of strong support from the majority owner, Government of India (GoI), and the bank's comfortable resource profile. The ratings also factor in stress on asset quality and resultant decline in the earnings profile due to high provisioning requirement.

Analytical Approach
For arriving at the ratings, CRISIL has factored in the support the bank is expected to receive from GoI. This is because GoI is both the majority shareholder in public sector banks (PSBs) and the guardian of India's financial system. The stability of the banking sector is of prime importance to GoI, given the criticality of the sector to the economy, the strong public perception of government backing for PSBs, and the severe implications of any PSB failure in terms of political fallout, systemic stability, and investor confidence in public sector institutions.

Key Rating Drivers & Detailed Description
Strengths:
*** Expectation of strong support from the majority owner, GoI**
The rating factors in expectation of 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. The stability of the banking sector is of prime importance to the government, given the criticality of the sector to the economy, the strong public perception of sovereign backing for PSBs, and the severe implications of any PSB failure in terms of political fallout, systemic stability, and investor

confidence in public sector institutions. The majority ownership creates a moral obligation on GoI to support PSBs, including Allahabad Bank.

As a part of the Indradhanush framework, the government had pledged to infuse at least Rs 70,000 crore in PSBs over fiscals 2015 to 2019, of which Rs 25,000 crore each was infused in fiscals 2016 and 2017. Further, in October 2017, the government had outlined a recapitalisation package of Rs 2.11 lakh crore over fiscals 2018 and 2019. In August 2019, the government announced the first round of capital infusion (of around Rs 55,250 crore) in 10 PSBs (of the total Rs 70,000 crore proposed for fiscal 2020). GoI infused Rs 11740 crore in Allahabad Bank in fiscal 2019.

*** Comfortable resource profile**
As a proportion of overall deposits, CASA deposits stood at 48.1% as on September 30, 2019, (49.5% as on March 31, 2019). The bank has strong CASA base on account of its branch network in the northern and eastern states. Resource profile should remain comfortable over the medium term, supported by the bank's well-established market position in central and eastern India, where a stable deposit base has been maintained.

Weaknesses:
*** Weak asset quality**
Asset quality remains under stress, with gross NPAs at 19.05% as on September 30, 2019, as against 17.55% as on March 31, 2019. Net NPAs has increased to 5.98% as on September 30, 2019, from 5.22% as on March 31, 2019. The bank's slippages (annualised) stood at 10% (Rs. 7125 crore) for H1FY20 (7.1% (Rs. 10726 crore) for fiscal 2019). Increase in slippages was driven by the agriculture segment (Rs. 3800 crore) in H1FY20. However, slippages in the corporate book has been on a declining trend with most of the stress in corporate book having been recognised. Nevertheless, performance of the agriculture and SME book will remain a monitorable. While the bank is focusing on improving its collection and recovery mechanism to improve its asset quality, its ability to control slippages and increase the loan portfolio to less risky segments remains a key monitorable over the medium term.

*** Weak earnings profile**
Earnings profile has been impacted by the deterioration in asset quality. The bank reported a net loss of Rs 1986 crore in half year ended in September 30, 2019, as against a loss of Rs. 3767 crore in in the corresponding period of the previous fiscal. Losses are largely on account of higher provisioning requirement; credit cost stood at 3.0% for the half-year ended September 30, 2019, as against 4.1% for the corresponding period of the previous fiscal. Nevertheless, provisioning coverage ratio (excluding technical write-offs) improved to 73.0% as on September 30, 2019, from 54.0% as on March 31, 2018. The bank reported a return on assets of -1.63% for half year ended in September 30, 2019 as against -3.16% for corresponding period of the previous fiscal. The ability of the bank to improve its asset quality, and hence profitability, is a key monitorable.

Liquidity Superior
The bank has superior liquidity, supported by a sizeable retail deposit base that forms a significant part of the total deposits. Liquidity coverage ratio was 161.6% as on September 30, 2019, against the regulatory requirement of 100%. The excess statutory liquidity ratio was 61.6% as on that date. The bank's liquidity also benefits from access to systemic sources of funds such as the liquidity adjustment facility from the Reserve Bank of India, access to the call money market, and refinance limits from sources such as National Housing Bank and National Bank for Agriculture and Rural Development.

Rating Sensitivity factors
Upward factors:
* Completion of the proposed amalgamation with Indian Bank
* Improvement in asset quality and profitability on a sustained basis

Downward factors:
* Higher than expected deterioration in asset quality thereby impacting earnings profile
* Decline in capital adequacy ratios below minimum regulatory requirements (including CCB, which is Tier I of 9.5% and overall CAR of 11.5% as on March 31, 2020) for an extended period

About the Bank
Founded in April 1865 by a group of Europeans in Allahabad (Uttar Pradesh), Allahabad Bank is a medium-sized public sector bank with an asset base of Rs 2.45 lakh crore, network of 3,174 domestic branches as on September 30, 2019.

In fiscal 2019, total income (net of interest expenses) was Rs 7,211 crore and net loss was Rs 8,334 crore against total income (net of interest expenses) of Rs 7,425 crore and a net loss of Rs 4,674 crore in fiscal 2018.

Total income (net of interest expenses) was Rs5,387 crore and net loss was Rs 4,500 crore in the nine months ended December 31, 2018, as against total income (net of interest expenses) of Rs6,054 crore and net loss of Rs 1,165 crore for the corresponding period in the previous fiscal.

Key Financial Indicators

As on / for the fiscal ended September 30		2019	2018
Total assets	Rs crore	245145	240987
Total income	Rs crore	9370	9205
Profit after tax	Rs crore	-1986	-3767
Gross NPA	%	19.1	17.5
Overall capital adequacy ratio	%	10.9	7.1
Return on assets	%	-1.7	-3.1

Any other information: Not applicable

Note on complexity levels of the rated instrument:
CRISIL complexity levels are assigned to various types of financial instruments. The CRISIL complexity levels are available on www.crisil.com/complexity-levels. Users are advised to refer to the CRISIL complexity levels for instruments that they consider for investment. Users may also call the Customer Service Helpdesk with queries on specific instruments.

Note on Tier-II Instruments (Under Basel III)
The distinguishing feature of Tier-II capital instruments under Basel II 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 Reserve Bank of India (RBI). CRISIL believes the PONV trigger is a remote possibility in the Indian context, given the robust regulatory and supervisory framework, and 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 hybrid Instruments (Under Basel II)

Given that hybrid capital instruments (Tier-I perpetual bonds and Upper Tier-II bonds; under Basel II) have characteristics that set them apart from Lower Tier-II bonds (under Basel II), the ratings on the two instruments may not necessarily be identical. The factors that could trigger a default event for hybrid instruments include: the bank breaching the regulatory minimum capital requirement, or the regulator's denial of permission to the bank to make payments of interest and principal if the bank reports losses. Hence, the transition from one rating category to another may be significantly sharper for these instruments than in the case of Lower Tier-II bonds; this is because debt servicing on hybrid instruments is far more sensitive to the bank's overall capital adequacy levels and profitability.

Annexure - Details of Instrument(s)

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs crore)	Outstanding rating with outlook
NA	Tier II Bonds (Basel III)*	NA	NA	NA	1500	CRISIL AA-/Watch Positive
INE428A08028	Tier II Bonds (Basel III) - Series I	20-Jan-15	8.78%	20-Jan-25	500	CRISIL AA-/Watch Positive
INE428A08044	Tier II Bonds (Basel III) - Series II	21-Dec-15	8.64%	20-Dec-25	1000	CRISIL AA-/Watch Positive
INE428A09117	Upper Tier II Bonds (Basel II) - Series II	18-Dec-09	8.58%	18-Dec-24	500	CRISIL A+/Watch Positive
INE428A09125	Tier I Perpetual Bonds (Basel II) - Series II	18-Dec-09	9.08%	NA	150	CRISIL A+/Watch Positive

*Yet to be issued

Annexure - Details of Rating Withdrawn

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs crore)
INE428A09083	Lower Tier II Bonds (Basel II) - Series VIII	26-Mar-09	9.23%	26-Mar-19	400
INE428A09109	Lower Tier II Bonds (Basel II) - Series IX	4-Aug-09	8.45%	4-Aug-19	450
INE428A09091	Tier I Perpetual Bonds (Basel II) - Series I	30-Mar-09	9.20%	NA	150
INE428A09075	Upper Tier II Bonds (Basel II) - Series I	19-Mar-09	9.28%	19-Mar-24	500

Annexure - Rating History for last 3 Years

	Current			2019 (History)		2018		2017		2016		Start of 2016
Instrument	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Lower Tier-II Bonds (under Basel II)	LT	0.00 17-12-19	CRISIL AA-/(Watch) Positive	05-09-19	CRISIL AA-/Negative	17-08-18	CRISIL AA-/Watch Negative	12-09-17	CRISIL AA-/Negative	04-11-16	CRISIL AA-/Negative	CRISIL AA+/Negative
				19-02-19	CRISIL AA-/Negative	21-05-18	CRISIL AA-/Watch Developing	17-02-17	CRISIL AA-/Negative	10-03-16	CRISIL AA/Negative	
						07-02-18	CRISIL AA-/Stable			16-02-16	CRISIL AA/Negative	
						25-01-18	CRISIL AA-/Stable					
Perpetual Tier-I Bonds (under Basel II)	LT	150.00 17-12-19	CRISIL A+/(Watch) Positive	05-09-19	CRISIL A+/Negative	17-08-18	CRISIL A+/Watch Negative	12-09-17	CRISIL A+/Negative	04-11-16	CRISIL A+/Negative	CRISIL AA/Negative
				19-02-19	CRISIL A+/Negative	21-05-18	CRISIL A+/Watch Developing	17-02-17	CRISIL A+/Negative	10-03-16	CRISIL AA-/Negative	
						07-02-18	CRISIL A+/Stable			16-02-16	CRISIL AA-/Negative	
						25-01-18	CRISIL A+/Stable					
Tier I Bonds (Under Basel III)	LT		--		--		--	17-02-17	Withdrawal	04-11-16	CRISIL A-/Negative	--
										10-03-16	CRISIL A/Negative	
										16-02-16	CRISIL A/Negative	
Tier II Bonds (Under Basel III)	LT	1500.00 17-12-19	CRISIL AA-/(Watch) Positive	05-09-19	CRISIL AA-/Negative	17-08-18	CRISIL AA-/Watch Negative	12-09-17	CRISIL AA-/Negative	04-11-16	CRISIL AA-/Negative	CRISIL AA+/Negative
				19-02-19	CRISIL AA-/Negative	21-05-18	CRISIL AA-/Watch Developing	17-02-17	CRISIL AA-/Negative	10-03-16	CRISIL AA/Negative	
						07-02-18	CRISIL AA-/Stable			16-02-16	CRISIL AA/Negative	
						25-01-18	CRISIL AA-/Stable					

Upper Tier-II Bonds (under Basel II)	LT	500.00 17-12-19	CRISIL A+/(Watch) Positive	05-09-19	CRISIL A+/Negative	17-08-18	CRISIL A+/Watch Negative	12-09-17	CRISIL A+/Negative	04-11-16	CRISIL A+/Negative	CRISIL AA/Negative
				19-02-19	CRISIL A+/Negative	21-05-18	CRISIL A+/Watch Developing	17-02-17	CRISIL A+/Negative	10-03-16	CRISIL AA-/Negative	
						07-02-18	CRISIL A+/Stable			16-02-16	CRISIL AA-/Negative	
						25-01-18	CRISIL A+/Stable					

All amounts are in Rs.Cr.

Links to related criteria
[Rating Criteria for Banks and Financial Institutions]
[Criteria for Notching up Stand Alone Ratings of Entities Based on Government Support]
[Rating Criteria for Hybrid Capital instruments issued by banks under Basel II guidelines]
[Rating criteria for Basel III - compliant non-equity capital instruments]

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