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India Ratings Upgrades Yes Bank to 'IND BBB'/Stable; Off RWE

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India Ratings and Research (Ind-Ra) has upgraded Yes Bank Ltd's Long-Term Issuer Rating to 'IND BBB' from 'IND BB-' while resolving the Rating Watch Evolving (RWE). The Outlook is Stable. The instrument-wise rating actions are as follows:

Instrument Type*	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Rating/Outlook	Rating Action
Infrastructure bonds	-	-	-	INR35.8	IND BBB/Stable	Upgraded; Off RWE
Basel III Tier 2 bonds	-	-	-	INR110	IND BBB-/Stable	Upgraded; Off RWE

*Details in Annexure

The multi-notch upgrade and the resolution of RWE reflects a significant improvement in Yes Bank's profile and operating metrics post its reconstruction in March 2020. The upgrade factors in the bank's substantial equity raise; reduced concerns on immediate liquidity position as its funding profile moves towards stability; a strengthened board, and limited incremental credit costs from identified delinquent assets, as the bank has ramped up its provision cover.

Ind-Ra expects the bank to continue improving its operating metrics and liability profile over the next few quarters as it continues making provisions for COVID-19 related impact on its portfolio. Ind-Ra also expects the bank to benefit from its association with its single largest shareholder the State Bank of India (SBI; 'IND AAA'/Stable). The agency believes it is critical for the bank to rebuild its loans and deposit franchise, as well as trust in the bank and its management to recover the bank's franchise.

KEY RATING DRIVERS

Reconstruction Exercise Measures Addresses Key Challenging Areas: In Yes Bank's regulator-driven reconstruction in March 2020, the bank received INR100 billion equity infusion from domestic banks, led by the SBI with INR60 billion for 48.21% stake. Most of the proceeds from this infusion as well as the write off of additional tier-1 bonds, of about INR85 billion, were used to boost provisions. The bank also received substantial liquidity support in the form of INR500 billion refinancing from the Reserve Bank of India (RBI) in March 2020 and liability support on certificates of deposit and interbank lines from the financial eco-system. As of end-July 2020, the bank had repaid 70% of the refinance lines to the RBI.

The bank has raised additional equity of INR150 billion since March 2020; the proforma common equity tier-1 (CET-1) of the bank for 1QFY21 was 13.4% (6.5% without adding the fresh equity raise).

The bank's new, post-reconstruction, board has two serving and one former officers from the SBI; the latter – Prashant Kumar- the former chief financial officer of the SBI and is now the chief executive officer of Yes Bank. The new board is focussed on improving governance and compliance; regaining its liability franchise, and building a sustainable loan and transaction business franchise.

The bank is also exploring hiving off a large portion of its non-performing assets and non-performing investment book into a separate legal unit to manage it more efficiently, release some capital and reduce the need for ageing-related provisions. Ind-Ra expects the bank's association with the SBI to help rebuild trust in the management as well as the overall institution of Yes Bank. Ind-Ra believes this could assist the bank to rebuild its liability and deposit profile, strengthen access to debt capital markets and interbank markets, and rebuild its franchise.

Strengthened Capital Buffers; Limited Incremental Credit Costs from Identified Stressed Assets: Yes Bank reported substantially better-than-historical levels of proforma CET-1 capital of 13.4% at end-1QFY21 (March 2020: 6.3%), and provision coverage ratio of 75% (2QFY20: 43%). As the bank has taken accelerated provisions on the majority of its stressed book, Ind-Ra expects marginal near-term ageing provision requirements, giving the bank the ability to build provisions for COVID-19 related stress. The agency believes the restructuring guidelines could help the bank manage its COVID-related stress and help spread its impact over two years.

Ind-Ra believes 7.7% of the banking system advances could be restructured in FY21 and the restructuring quantum could be greater, given its higher exposure to real estate, hospitality and micro, small and medium enterprises.

The bank has residual/legacy additional tier-1 bonds and upper tier-2 bonds, whose coupons the bank was unable to pay in 4QFY20 and 1QFY21 as it was not compliant with the minimum capital and profitability levels. Post the capital infusion, the bank was able to pay the cumulative coupons on the upper tier-2 bonds. Ind-Ra believes the bank will be able to service these coupon payments as it is in compliance with the capital requirement and will post modest profits in FY21.

Operating Performance likely to Improve Gradually: In the medium term, the bank will focus on the resolution of corporate stressed assets, non-corporate segments and transaction banking, mainly in the corporate segment, to generate current account float and granular fee income streams. This, the agency believes, along with a changing portfolio mix - large corporate portfolio expected to constitute 40% of the bank's advances in the medium term (1QFY21: 55%) - could offset the declining yields on the portfolio.

The bank is offering 1.5%-2% higher deposit rates than other higher-rated private sector banks. The agency believes the bank's non-interest income stream and current account deposit accretion could have adverse impactd by the new RBI circular, which states that CA accounts can be opened in lending banks.

Ind-Ra expects the bank's pre-provision operating profits to be between 2.5%-3% in the medium term while credit costs could be 2%-2.5%, assuming the bank will continue building up provisions for the assets expected to be restructured under the restructuring guidelines. The aforementioned factors, along with the lower requirement of ageing provisions and restructuring viable stressed assets gives the bank financial ability and time to make provisions for stressed assets in a post-COVID-19 environment. Hence, Ind-

Ra expects the bank to post modest profits in FY21.

Liquidity Indicator – Adequate: As the bank is building back its liabilities and deposit profile, it has also complied with statutory liquidity ratio (SLR) and liquidity coverage ratio requirements; its SLR improved above-regulatory compliance levels (March 2020: 10%) and liquidity coverage ratio to about 114% at end-June 2020 (40.4%). The bank has made a provision of INR3.3 billion for SLR non-compliance and would be required to pay the same to the RBI, if required.

The bank's short-term liabilities exceeded the short-term assets by 15% of total assets at end-June 2020 and is manageable in the agency's opinion. Most of this gap is on account of the scheduled repayment of INR450 billion to the RBI in 2QFY21, part of which has already been repaid. With low growth in advances, Ind-Ra expects the deposit pricing to help the bank manage the tenor of liabilities and improve the balance sheet liquidity position while providing the bank with time to enhance access to interbank and debt capital markets.

RATING SENSITIVITIES

Positive: A sustained increase in the franchise scale, along with a considerable improvement in the retail franchise with a more granular funding and asset mix, while building stronger capital and operating buffers, could lead to a positive rating action.

Negative: A significantly higher-than-expected deterioration in the asset quality owing to COVID-19 and impairment in the funding profile could lead to a negative rating action. A sizeable drop in the provision coverage ratio will also lead to a negative rating action. CET-1 reducing below 10% and the premature withdrawal of support by the banking system could also lead to negative rating action.

COMPANY PROFILE

Yes Bank was established in 2004 as a new-generation private sector bank, headquartered in Mumbai. It was incorporated in 2004 and has grown to become a full service commercial bank, providing complete range of products, services and digital offerings, catering to corporate, micro, small and medium enterprises and retail customers.

FINANCIAL SUMMARY

Particulars (INR billion)	**FY20**	**FY19**
Total assets	2,578.3	3,808.26
Total equity	217.3	269.04
Net income	-227.2*	17.20
Return on assets (%)	-7.1*	0.5
CET-1 (%)	6.3	8.4
Source: YES Bank *Excluding proceeds from write off of additional tier-1 bonds		

RATING HISTORY

Instrument Type	**Current Rating/Outlook**			**Historical Rating/Rating Watch/Outlook**						
	Rating Type	**Rated Limits (billion)**	**Rating**	**18 March 2020**	**6 March 2020**	**12 February 2020**	**18 December 2019**	**31 August 2019**	**8 May 2019**	**2 November 2018**
Issuer rating	Long-term/Short-term	-	IND BBB/Stable	IND BB-/RWE	IND BB-/RWN	IND A-/RWN	IND A/RWN/IND A1/RWN	IND A+/Negative/IND A1+	IND AA-/Negative/IND A1+	IND AA+/Negative/IND A1+
Basel III Tier 2 Bonds	Long-term	INR110	IND BBB-/Stable	IND B+/RWE	IND B+/RWN	IND A-/RWN	IND A/RWN	IND A+/Negative	IND AA-/Negative	IND AA+/Negative
Infrastructure bonds	Long-term	INR35.8	IND BBB/Stable	IND BB-/RWE	IND BB-/RWN	IND A-/RWN	IND A/RWN	IND A+/Negative	IND AA-/Negative	IND AA+/Negative

ANNEXURE

Issue name/Type	**ISIN**	**Date of Issuance**	**Coupon Rate (%)**	**Maturity Date**	**Size of Issue (billion)**	**Rating/Rating Watch**
Infrastructure bonds	INE528G08360	29 December 2016	7.62	29 December 2023	INR3.3	IND BBB/Stable
Total utilised					**INR3.3**	
Total unutilised					**INR32.5**	
Basel III Tier 2 Bonds	INE528G08378	29 September 2017	7.8	29 September 2027	INR25	IND BBB-/Stable
Basel III Tier 2 Bonds	INE528G08386	3 October 2017	7.8	1 October 2027	INR15	IND BBB-/Stable
Basel III Tier 2 Bonds	INE528G08402	22 February 2018	8.73	22 February 2028	INR30	IND BBB-/Stable
Basel III Tier 2 Bonds	INE528G08410	14 September 2018	9.12	15 September 2028	INR30.42	IND BBB-/Stable
Total utilised					**INR100.42**	
Total unutilised					**INR9.58**	

COMPLEXITY LEVEL OF INSTRUMENTS

For details on the complexity level of the instruments, please visit https://www.indiaratings.co.in/complexity-indicators.

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Applicable Criteria

Financial Institutions Rating Criteria
Rating Bank Subordinated and Hybrid Securities

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