CSB Bank

SEC/292/2023

August 18, 2023

BSE Limited,
Phiroze Jeejeebhoy Towers,
Dalal Street,
Mumbai 400001.
Scrip code: 542867

National Stock Exchange of India Ltd.,
Exchange plaza, 5th floor,
Bandra-Kurla Complex,
Bandra (E), Mumbai 400051.
Symbol: CSBBANK

Dear Sir/Madam,

Reaffirmation of Rating by India Ratings & Research

Pursuant to Regulation 30 of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, we wish to inform you that, India Ratings & Research, vide letter dated August 17, 2023, has reaffirmed its rating of 'IND A' with Outlook Stable, to the Rs. 500 Crore, Basel III- compliant Tier II bonds issue Programme of the Bank. The Bank has not yet issued bonds as part of the programme.

The rating rationale provided by India Ratings & Research is enclosed herewith.

Kindly take the same on record.

Thanking You.

Yours faithfully,

SIJO VARGHESE

Digitally signed by SIJO VARGHESE
DN: st=KERALA, serialNumber=da67d16a892dbce0f63c24da300ebd6a93ef99e00629fb3f519fd7bc49a7ccee, postalCode=680020, ou=BOARD & SHARES DEPARTMENT, o=CSB BANK LTD, c=IN, cn=SIJO VARGHESE
Date: 2023.08.18 15:25:02 +05'30'

Sijo Varghese
Company Secretary

India Ratings & Research
A Fitch Group Company

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India Ratings Affirms CSB Bank's Tier II Bonds at 'IND A'; Outlook Stable

Aug 17, 2023 | Private Sector Bank

India Ratings and Research (Ind-Ra) has affirmed CSB Bank Limited's (CSB) Tier II bonds as follows:

Instrument Type	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Rating/Outlook	Rating Action
Basel III-complaint Tier II bonds*	-	-	-	INR5.0	IND A/Stable	Affirmed

* Yet to be issued

Key Rating Drivers

Sustained Healthy Capital Buffers: CSB's common equity tier 1 (CET1) remained comfortable at 24.8% in 1QFY24 (FY23: 25.9%; FY22: 24.4%) on the back of adequate profitability with return on assets at 1.8% (2.06%, 1.90%, FY21:1%). Its risk weight optimisation (RWA) to advances stood at 54% in FY23 (FY22: 60%), against 69% in FY19. The healthy capital levels are substantially aided by gold loans that typically have low risk weights and the fact that about 70% of the advances in the corporate segment are rated above 'A' category. The bank plans to maintain over 45% of its advances in gold loan product over the near-to-medium term, and hence, a substantial portion of this capital benefit could continue.

However, Ind-Ra believes the newer products introduced recently and expected to be introduced in the near term could witness a material traction FY25 onwards. The equity/advances was 15.5% at FYE23 (FYE22: 16.8%; FYE21: 15%). In Ind-Ra's opinion, the bank has a reasonable ability to raise additional equity from the market, if needed.

Stable Deposit Profile; Franchise Building outside Kerala and Tamil Nadu to be Seen: The bank's total deposits grew 21% yoy to INR244.8 billion in 1QFY24 (FY23: INR245 billion; FY22: INR201.9 billion). Ind-Ra opines that the bank has one of the lowest cost of deposits among the mainstream commercial banks, benefiting from a sticky depositor base. CSB's current account deposits as a percentage of deposits is lower than most mainstream banks since it has a limited franchise. CSB has taken several initiatives towards building a pan-India franchise such as opening branches outside Kerala and Tamil Nadu, and expanding its product portfolio. The bank's non-resident external deposits constituted over 20% of the total deposits in FY23due to its legacy of being a community-driven bank and having a presence in remittances (especially from non-resident Indians in the Middle East). The bank's current account savings account ratio was 32.18% in FY23 (FY22: 33.7%; FY21: 32.2%; FY20: 29.2%), post which it declined slightly to 30.84% in 1QFY24, due to a higher traction in term deposits supported by higher interest rates consequent to the increase in policy rates during the year. The bank's resource profile is favourable, compared with its peers'; the cost of deposits increased but remained lower than peers at 5% in 1QFY24 (FY23: 4.38%; FY22: 4.31%).

The share of deposits above INR20 million increased to 26% in FY23 (FY22: 15.6%, FY21: 12.6%). In addition, almost 55% of the bank's total deposits are from Kerala (FY22: 62%) and about 73% from the top two states (Kerala and Tamil Nadu; 77%). The bank set up 100 branches in FY23 and plans to set up another 100 in FY24. The new branches, as and when mature, will begin delivering granular deposits as well as reduce the bank's dependence on its top two states. Given CSB's low-cost of deposits and its plans to ramp up loans through new products over the medium term, if the traction on the deposit side is lower than advances over the near-to-medium term, either the deposit rates will need to be ramped up faster than peers' and/or the bank will need to look at wholesale deposits/borrowings.

Mid-term Strategy to drive Profitability in Long term The bank operates mainly in the granular retail segments that are often characterised by relatively higher yields. While the bank plans to grow its corporate book (mid-corporates and to some extent large corporates), this is likely to be a slow process as the size of capital limits the high exposures it can take and the higher cost of funds than peers. Further, CSB plans to increase its presence in the housing finance segment and loan against property segment, which could impact the yields adversely but improve its portfolio risk profile. However, build-up of the retail book of about 30%, a reduction of gold loan concentration in the portfolio mix and establishing as a national brand among others, will only be achievable over the long term.

The bank expects to maintain gold loans at 40%-45% of the total advances over the near-to-medium term. This portfolio is not prone to high credit costs as these costs emanate mostly from the non-gold portfolio. Restructured assets stood low at INR0.24 billion as of 1QFY24 (below 0.5% of gross advances). The agency estimates the bank to maintain 1.5%-1.7% of return on assets annually over the medium term. The operating costs are likely to increase modestly over the near-to-medium term, as the bank continues to open new branches in FY24 and invest in technology, systems and processes for new/revamping of existing products. The bank also saw a material contribution to its pre-provision operating profit from the recoveries from written off assets (mostly legacy non-performing assets). However, Ind-Ra expects the recoveries to decline in FY24 as the recoverable pool becomes smaller.

Fairfax Presence - a Positive: The presence of FIH Mauritius Investments Limited (FIH; Fairfax Holdings company), as a large investor (49% stake at 1QFYE24), not only provided CSB with about INR12 billion of equity leading to the write-off of legacy non-performing assets mostly by end-FY19, but also enhances the bank's capability to attract talent and improve governance through the implementation of best practices. CSB also benefits from the various forms of support generally available with the backing of large investor with pedigree. The bank has, over the past two years, appointed many senior management personnel and is likely to build upon on teams over the medium term. This, along with a clean balance sheet, enables CSB to expand beyond its comfort zone in terms of geography, scale and products. While Ind-Ra believes CSB might not require capital support from its parent in a normal business scenario, it expects the key shareholder to provide support to the extent possible within the regulatory contours and its dilution commitment to the regulator.

Liquidity Indicator - Adequate: The bank's one-year cumulative surplus (assets less liabilities maturing in one year) was about 34% of the total inflow at FYE23. This also factors in almost 90% renewal rate of their term deposits, which is higher than some of the larger banks'. The liquidity coverage ratio stood at 107% at 1QFYE24 (FYE23: 123%; FYE22: 154%), which the bank expects to increase in the near term. CSB has about INR17.1 billion as excess statutory liquidity ratio investments (mostly in liquid investments where modified duration is less than one year) for liquidity support. The bank's deposit rates are comparable to those of higher rated banks despite its savings account rates being lower than even some of the higher rated banks'.

Reducing Regional Concentration Work in Progress: CSB's deposit profile is regionally concentrated with Kerala, Tamil Nadu, Maharashtra and Karnataka together contributing 90% to the total deposits, including the non-resident external deposits at end-4QFY23. Among these states, the bank is majorly dependent on Kerala and Tamil Nadu for deposits as well as advances. Of the 100 newly opened branches in FY23, majority are outside Kerala and Tamil Nadu. Also, most of the 100 branches will be set up outside Kerala and Tamil Nadu in FY24.

Modest-sized Franchise with Evolving Asset Mix: CSB has a modest franchise in southern India states with an overall share in advances and deposits of less than 0.5%. At FYE23, the bank's portfolio mix consisted 45% gold loans (FYE22: 39%), 12% small and medium enterprises loans (15%; mostly legacy), 14% agri & retail loans (14%), and 29% corporate and other loans (32%). The top 20 exposures accounted for about 10.4% of the total exposure at FYE23 (FYE22: 13.6%). The bank has expanded its product suite and revamped its credit policies on various products over the last two-to-three years. Further, it has set targets up to FY30 as part of the 2030 vision approved by the board.

CSB is building scale in most of the products, including retail segments (home loans, loans against property, personal/consumer loans, auto loans, among others). Most of these segments are small and will take some time to achieve a material scale and seasoning. The bank is likely to continue to focus on gold loans to keep benefitting from higher yields, low credit costs and lower risk weights over the medium term. Over the long-term, the bank aims to become a mid-sized bank with pan-India presence and a diversified portfolio mix with gold loan portfolio of below 20%.

Rating Sensitivities

Positive: A substantial increase in the franchise, experience in corporate assets, strengthening and improvement of the deposit profile, especially outside Kerala and Tamil Nadu, a scaling up of non-gold loans materially and consistent profitability ratios could lead to a positive rating action.

Negative: The bank’s CET1 falling below 13%, equity erosion or slippages in non-gold portfolio, and restructured assets exceeding 5% on a sustained basis could lead to a negative rating action.

ESG Issues

ESG Factors Minimally Relevant to Rating: Unless otherwise disclosed in this section, the ESG issues are credit neutral or have only a minimal credit impact on CSB, due to either their nature or the way in which they are being managed by the entity. For more information on Ind-Ra’s ESG Relevance Disclosures, please click here. For answers to frequently asked questions regarding ESG Relevance Disclosures and their impact on ratings, please click here.

Company Profile

CSB was established in 1920 as The Catholic Syrian Bank Limited. It is the oldest private sector bank in Kerala with 706 branches at 1QFYE24.

FINANCIAL SUMMARY

Particulars	**FY23**	**FY22**
Total assets (INR billion)	291.6	253.6
Total net worth (INR billion)	32.03	26.5
Net profit (INR billion)	5.47	4.58
Return on assets (%)	2.06	1.90
Common equity tier 1 ratio (%)	25.9	24.4
Capital adequacy ratio (%)	27.1	25.9
Source: CSB		

Non-Cooperation with previous rating agency

Not applicable

Rating History

Instrument Type	**Current Rating/Outlook**			**Historical Rating/Outlook**	
	Rating Type	**Rated Limits (billion)**	**Rating**	**18 August 2022**	**19 August 2021**
Basel III-complaint Tier II bonds	Long-term	INR5.0	IND A/Stable	IND A/Stable	IND A/Stable

Complexity Level of Instruments

Instrument Type	Complexity Indicator
Basel III tier 2 bonds	Moderate

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

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APPLICABLE CRITERIA

Rating Bank Subordinated and Hybrid Securities

Financial Institutions Rating Criteria

Evaluating Corporate Governance

The Rating Process

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