Rating Rationale

August 22, 2023 | Mumbai

UCO Bank

Rating Reaffirmed; Lower Tier-II Bonds (under Basel II) Withdrawn

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Rating Action

Rs.1000 Crore Lower Tier-II Bonds (under Basel II)	**CRISIL AA-/Stable (Withdrawn)**
Rs.10000 Crore Certificate of Deposits	**CRISIL A1+ (Reaffirmed)**

Note: None of the Directors on CRISIL Ratings Limitedâ€™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 reaffirmed its short-term rating on the certificate of deposit programme of UCOÂ Bank at â€˜CRISIL A1+â€™.

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CRISIL Ratings has also **withdrawn** its long-term rating on the Rs 1,000 crore Lower Tier-II bonds (Basel II) at the bankâ€™s request as the same is redeemed on maturity and on receipt of confirmation from the debenture trustee (see Annexure - Details of Rating Withdrawn). The withdrawal is in line with CRISIL Ratingsâ€™ withdrawal policy.

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The rating factors in the enhancement in asset quality and profitability of the bank. Asset quality improved with reported gross non-performing assets (NPAs) at 4.78% as on March 31, 2023 (4.48% as on June 30, 2023), from 7.89% a year earlier, supported by lower slippages. Net NPAs declined substantially and stood at 1.18% as on June 30, 2023. As on March 31, 2023, restructured advances accounted for 2.9% of the bank portfolio.

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Improvement in asset quality led to better profitability. Return on asset (RoA) increased to 0.65% in fiscal 2023 (0.30% annualised for the three months ended June 30, 2023) from 0.36% in fiscal 2022 since credit cost reduced to 0.51% from 1.17%.

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The overall rating continues to reflect the expectation of strong support from the Government of India (GoI) and moderate resource profile. These strengths are partially offset by average, albeit improving, asset quality and earnings

Analytical Approach

CRISIL Ratings has considered the standalone business and financial risk profiles of UCO Bank and has factored in the expected strong government support.

Key Rating Drivers & Detailed Description

Strengths:

Expectation of strong support from GoI

The government should continue to provide strong support both on an ongoing basis and in the event of distress. This is because, GoI is 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, considering the sectorâ€™s criticality to the economy, the strong public perception of sovereign backing for PSBs, and adverse implications of any PSB failure, in terms of political fallout, systemic stability, and investor confidence. The majority ownership creates a moral obligation on the government to support PSBs, including UCO Bank.

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GoI has supported UCO Bank with infusion of Rs 22,645 crore over fiscals 2016-2022. Of this, Rs 2,600 crore was infused in fiscal 2021; consequently, tier 1 and capital-to-risk weighted assets ratio (CRAR) were at 11.14% and 13.74%, respectively, as on March 31, 2021. Tier 1 and CRAR have shown healthy year on year (y-o-y) growth and were 13.96% and 16.51%, respectively, as on March 31, 2023, supported by growth in profitability. Tier 1 and CRAR were 14.16% and 16.85%, respectively, as on June 30, 2023.

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Moderate resource profile

Total deposits increased 11% y-o-y to Rs 2,49,338 crore as on March 31, 2023 (Rs 2,49,694 crore as on June 30, 2023). Ratio of current account and savings account (CASA) deposits to total deposits was 36.70% as on June 30, 2023, and 36.79% as on March 31, 2023. Of the CASA deposits, saving deposits accounted for 89%, and current deposits for the remaining 11%. Additionally, cost of deposits inched up to 4.06% in fiscal 2023 from 3.81% in fiscal 2022.

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The bank should maintain its resource profile, supported by its established market position in eastern India, which has helped maintain a stable deposit base.

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Weakness:

Average, albeit improving, asset quality and profitability

Asset quality remains average, albeit it improved in fiscal 2023 with gross NPAs at 4.78% as on March 31, 2023, (4.48% as on June 30, 2023), as compared with 7.89% a year ago. The improvement was driven by lower slippages of Rs 2,096 crore in fiscal 2023 from Rs 6,123 crore in fiscal 2022 (Rs 536 crore in the first three months of fiscal 2024). Slippages to net advances were 1.71% in fiscal 2023 and 1.38%[1] in the three months ended June 30, 2023. Majority of stress in the corporate book is already recognised, and fresh slippage in this segment is expected to be relatively low. As on March 31, 2023, restructured advances accounted for 2.9% of the bank portfolio, and NPAs in the restructured book were 13.44%. Net NPAs were 1.29%% as on March 31, 2023, (1.18% as on June 30, 2023) from 2.7% a year ago.

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The strategy to grow more granular assets in the retail, and micro, small and medium enterprise (MSME) segments, and adoption of a conservative approach while lending to corporates, augurs well for the asset quality. Also, the increasing proportion of high-yield retail, agriculture, and MSME segments have resulted in steady improvement in net interest margin to 2.58% in fiscal 2023 (2.65% for the three months ended June 30, 2023) from 2.48% in fiscal 2022. Profitability has further benefitted from lower credit cost, which reduced to 0.51% from 1.17%% for the same comparative period. RoA was 0.65% in fiscal 2023, up from 0.36% in fiscal 2022, and net profit was Rs 1,862 crore from Rs 930 crore.
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Net profit was Rs 223 crore (annualised RoA 0.30%) during the three months ended June 30, 2023. Bank maintained a healthy provision cover of 74.5% as on June 30, 2023.
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Nevertheless, the ability to manage collections and control credit costs, particularly that from the restructured book, and improving profitability will remain key monitorables.

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[1]*Annualised, Slippage ratio= Slippages in Q1FY24/ Net Advances as on March 31, 2023*

Liquidity: Strong
Liquidity remains supported by the strong retail deposit base. The liquidity coverage ratio stood at 178.9% as on March 31, 2023 and was higher than the regulatory requirement. The excess statutory liquidity stood at Rs 23,518 crore (around 9.61% of net demand and time liabilities) as on March 31, 2023. Liquidity benefits from access to systemic sources of funds, such as the liquidity adjustment facility from the Reserve Bank of India and call money market.
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ESG profile
CRISIL Ratings believesÂ theÂ Environment, Social andÂ Governance (ESG) profileÂ ofÂ UCO Bank supports its already strong credit risk profile.
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The ESG profile for financial sector entities typically factors in governance as a key differentiator. The sector hasÂ aÂ reasonable social impact because of its substantial employee and customer base and can play a key role in promoting financial inclusion. WhileÂ the sector does not haveÂ aÂ direct adverse environmental impact, the lending decisions may have a bearing on the environment.
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UCO Bank has an ongoing focus on strengthening the various aspects of its ESG profile.
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Key ESG highlightsÂ ofÂ UCO Bank:
- ESG disclosures of the bank are evolving, and it is in the process of further strengthening the disclosures going forward.
- The bank has started focusing on paperless banking and has a policy of not lending to industries consuming / producing Ozone Depleting Substance (ODS)
- As on March 31, 2023, aroundÂ 28.33% of the bankâ€™s total workforce comprisedÂ women employees, and itÂ has taken initiatives to promote gender equality within the organisation.
- Of the board members, 38% are independent directorsÂ with none of them having a tenure exceeding 10 years.Â The bank also has a dedicated investor grievance redressal mechanism.

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There is growing importance of ESG among investors and lenders.Â TheÂ commitmentÂ ofÂ UCO Bank to ESG will play a key role in enhancing stakeholder confidence, given shareholding by foreign portfolio investors and access to domestic capital markets

Rating Sensitivity Factors
Downward Factors
- Material reduction in shareholding and/or expectation of support from GoI
- Decline in the capital adequacy ratio (CAR) to below minimum regulatory requirements (including capital conservation buffer, which is tier I of 9.5% and overall CAR of 11.5%)
- Continuous losses and sustained deterioration in asset qualitz.

About the Bank
UCO Bank was founded in 1943 as United Commercial Bank. It was renamed as UCO Bank by an Act of Parliament in 1985. In 2003, the bank made its initial public offering, resulting in dilution of government ownership. GoI owned 95.39% stake in the bank as on June 30, 2023. As on June 30, 2023, the bank had total advances and deposits of Rs 1,64,278 crore and Rs 2,49,694 crore, respectively.
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Profit after tax (PAT) was Rs 1,862 crore and total income (net of interest expenses) was Rs 9,852 crore in fiscal 2023, as against a net profit of Rs 930 crore and total income (net of interest expenses) of Rs 9,574 crore for fiscal 2022.

Key Financial Indicators

Particulars	Unit	Q1FY24	Q1FY23
Total assets	Rs crore	3,04,474	2,67,449
Total income (net of interest expense)	Rs crore	2,642	1,595
PAT	Rs crore	223	124
Gross NPA	%	4.48	7.42
Overall capital adequacy ratio	%	16.85	14.13
Return on assets*	%	0.30	0.18

**annualised*

Any other information: Not applicable

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 -Â Details of Instrument'Â in this Rating Rationale.

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Annexure - Details of Instrument(s)

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs.Crore)	Complexity level	Rating outstanding with outlook
NA	Certificates of deposit	NA	NA	7 to 365 Days	10,000	Simple	CRISIL A1+

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AnnexureÂ -Â Detail ofÂ RatingÂ Withdrawn

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs.Crore)	Complexity level	Rating outstanding with outlook
INE691A09185	Lower Tier II bonds (under Basel II)	28-Dec-2012	9.00%	28-Dec-2022	1000	Complex	Withdrawn

Annexure - Rating History for last 3 Years

Â	Current			2023 (History)		2022Â		2021Â		2020Â		Start of 2020
Instrument	**Type**	**Outstanding Amount**	**Rating**	**Date**	**Rating**	**Date**	**Rating**	**Date**	**Rating**	**Date**	**Rating**	**Rating**
Certificate of Deposits	ST	10000.0	CRISIL A1+	Â	--	25-08-22	CRISIL A1+	31-08-21	CRISIL A1+	31-08-20	CRISIL A1+	CRISIL A1+
Lower Tier-II Bonds (under Basel II)	LT	1000.0	Withdrawn	Â	--	25-08-22	CRISIL AA-/Stable	31-08-21	CRISIL A+/Positive	31-08-20	CRISIL A+/Stable	CRISIL A+/Stable
Upper Tier-II Bonds (under Basel II)	LT	Â	--	Â	--	Â	--	Â	--	31-08-20	Withdrawn	CRISIL A/Stable

All amounts are in Rs.Cr.

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Criteria Details

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

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