੧ੴ ਸ੍ਰੀ ਵਾਹਿਗੁਰੂ ਜੀ ਕੀ ਫਤਹ ॥

पंजाब एण्ड सिंध बैंक
Punjab & Sind Bank
ਪੰਜਾਬ ਐਂਡ ਸਿੰਧ ਬੈਂਕ
पी.एस.बी. (भारत सरकार का उपक्रम/A Govt. of India Undertaking)

प्र. का. लेखा एवं लेखा परीक्षा विभाग
"शेयर कक्ष" ,बैंक हाऊस, प्रथम तल,
21, राजेन्द्रा प्लेस, नई दिल्ली-110 008
H.O. Accounts & Audit Department
"Shares Cell", Bank House, 1st Floor,
21, Rajendra Place, New Delhi - 110008

Phone : 011-25782926, 25812922, 25817353, 25728930, Email:complianceofficer@psb.co.in

सदर्भ:................................ दिनांक /Dated:................................

Ref: PSB/HO/Shares Cell/ /2020-21 **April 27, 2020**

To,

National Stock Exchange of India Ltd.,
Exchange Plaza, C – 1, Block – G,
Bandra Kurla Complex, Bandra (East),
Mumbai – 400 051.
SYMBOL: PSB SERIES: EQ

Dear Sir,

Reg: Clarification

This has reference to your mail dated 23.04.2020, regarding clarification sought with respect to our announcement dated 21.04.2020 regarding Credit Rating.

Please find below our point wise reply:

1. **Whether promptly notified the Exchange, not later than 24 hours** – Yes
2. **In case of downward rating, the reasons published by rating agency for such downward rating** – Please refer the rating rationale provided by ICRA for details of the reasons for downgrade of the rating. The same is also available on the website of ICRA.

Yours faithfully,

Authorized Signatory

April 23, 2020

Punjab & Sind Bank: Long-term ratings downgraded to [ICRA]AA-(Negative)/[ICRA]A-(hyb)(Negative); short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Basel II Compliant Lower Tier II Bonds	200.00	0.00	[ICRA]AA-(Negative); Downgraded from [ICRA]AA(Negative) and Withdrawn
Basel II Compliant Lower Tier II Bonds	300.00	300.00	[ICRA]AA-(Negative); Downgraded from [ICRA]AA(Negative)
Basel III Compliant Tier I Bonds	1,000.00	1,000.00	[ICRA]A-(hyb)(Negative); Downgraded from [ICRA]A+(hyb)(Negative)
Certificates of Deposit Programme	10.000.00	10.000.00	[ICRA]A1+; Reaffirmed
Total	**11,500.00**	**11,300.00**	

**Instrument details are provided in Annexure-1*

The rating for the Basel III compliant Tier-I bonds (AT-I bonds) is three notches below the Tier-II bonds of the bank as these instruments have the following loss-absorption features that make them riskier:

- Coupon payments are non-cumulative and discretionary, and the bank has full discretion, at all times, to cancel coupon payments. Cancellation of discretionary payments shall not be an event of default.
- Coupons can be paid out of current year profits. However, if the current year profit is not sufficient or if the payment of the coupon is likely to result in a loss, the payment can be made through reserves and surpluses[1] created through the appropriation of profits (including statutory reserves). As per ICRA's estimates, these reserves and surpluses stood at 2.5% of the risk-weighted assets (RWAs) as on December 31, 2019 (3.1% as on March 31, 2019). However, the coupon payment is subject to the bank meeting the minimum regulatory requirements for CET I, Tier I and total capital ratios (including capital conservation buffer, CCB) at all times, as prescribed by the Reserve Bank of India (RBI) under Basel III regulations.

These Tier-I bonds are expected to absorb losses through the write-down mechanism at the objective pre-specified trigger point fixed at the bank's CET I ratio as prescribed by the RBI – 5.5% till September 29, 2020, and thereafter 6.125% of the total RWAs of the bank or when the point of non-viability (PoNV) trigger is breached, in the RBI's opinion.

The letters 'hyb', in parenthesis, suffixed to a rating symbol stand for hybrid, indicating that the rated instrument is a hybrid subordinated instrument with equity-like loss-absorption features. Such features may translate into higher levels of rating transition and loss severity vis-à-vis conventional debt instruments.

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[1] Calculated as per the amendment in the Basel III capital regulations for AT-I bonds by the RBI, vide its circular dated February 2, 2017;
as per the amended definition, distributable reserves include all reserves created through appropriations from the profit and loss account

Rationale

The rating downgrade factors in the continued weakness in the operating and financial risk profile of Punjab & Sind Bank (P&SB) despite the capital infusion by the Government of India (GoI) in FY2020. The bank reported sizeable losses before tax in 9M FY2020, which surpassed the capital infusion of Rs. 787 crore by the GoI and Rs. 100-crore equity capital raised via the employee share purchase scheme (ESPS). The rating downgrade also factors in the weak asset quality profile, with a high fresh slippage rate of 6.7% of standard advances in 9M FY2020 (5.9% in FY2019), due to large exposures to a few non-banking financial companies (NBFCs). This also resulted in elevated credit provisions, losses and a further increase in the net NPA%, which remains above the threshold of 6.0% for inclusion under the RBI's prompt corrective action (PCA) framework.

With erosion in its capital and an increase in the net NPAs, P&SB's solvency profile (net NPA/core equity) deteriorated to 125.3% as on December 31, 2019 from 109.4% as on March 31, 2019 and is expected to remain weak in FY2021 if the bank does not raise capital. Amid the slowing economic growth and the expected stress on the asset quality because of Covid-19, the fresh slippages are expected to remain high in FY2021. With an estimated gross fresh slippage of 4.5-5.5% in FY2021 and a provision cover of 60-61% by March 2021 to bring the net NPAs below the PCA threshold, ICRA estimates the bank's equity capital requirement at Rs. 1,500-2,000 crore (130-180% of the current market capitalisation). This will also translate into losses in FY2021, with a negative RoA of 0.7-0.8%, and this will be the fourth consecutive year of losses. The GoI has not budgeted any capital for public sector banks (PSBs) for FY2021 and hence the ability of the bank to raise capital will remain a challenge unless the GoI makes an announcement regarding capital infusion at a later date.

The ratings remain supported by P&SB's sovereign ownership (the GoI had a stake of 83.06% as on December 31, 2019), the demonstrated capital support by the GoI and the expectation of continued support, going forward. The ratings further consider P&SB's established presence and branch network in North India and strong liquidity profile, supported by a stable retail deposit base, large holdings of liquid government securities and a comfortable liquidity coverage ratio (LCR).

The rating of the AT-I bonds is three notches lower than the Tier-II bonds, given the expectation of continued losses, weak capital ratios and a further decline in the distributable reserves that are critical to service the coupon on these bonds. As per ICRA's estimates, the distributable reserves are expected to be 2.5% of RWAs as on December 31, 2019 and will decline further by the end of FY2021 to 0.4-1.0% of RWAs.

The outlook on the long-term ratings remains Negative on account of a weak outlook on the asset quality, profitability and solvency profile, translating into a large capital requirement for the bank.

Key rating drivers and their description

Credit strengths

Sovereign ownership with demonstrated capital support – P&SB has a majority sovereign ownership with the GoI's equity stake in the bank at 83.06% as on December 31, 2019. In FY2020, P&SB received Rs. 787 crore of equity capital from the GoI as a part of the Rs. 70,000-crore recapitalisation plan for PSBs. Driven by this, the shareholding increased to the current level from 80.28% as on September 30, 2019. Earlier in FY2018, the bank had received Rs. 785 crore as a part of the GoI's recapitalisation package for PSBs. ICRA expects the bank to need equity capital of Rs. 1,500-2,000 crore to meet the regulatory requirements. However, since the GoI has not budgeted any capital for PSBs for FY2021, capital raising for P&SB will remain a challenge unless the GoI makes an announcement regarding capital infusion at a later date.

Established presence in North India – P&SB has a long and established presence in North India, depicted by its network of 1,521 branches and 1,047 ATMs as on December 31, 2019 against 1,518 branches as on December 31, 2018 (1,506 branches as on December 31, 2017). Given the pressure on the bank's operating profitability, the branch expansion has remained limited over the last couple of years. However, given the retail presence, P&SB witnessed good growth in retail deposits (14% YoY as on December 31, 2019) and a modest increase in low-cost savings deposits (8% YoY as on December 31, 2019).

Credit challenges

Large-ticket corporate slippages result in further deterioration in asset quality profile in 9M FY2020; asset quality pressure likely to persist in FY2021 as well – P&SB's asset quality profile weakened further in 9M FY2020, with a high annualised fresh slippage rate of 6.7% compared to 5.9% in FY2019, largely attributable to large-ticket exposure to few NBFCs getting classified as non-performing during the period. Despite the sizeable write-offs undertaken by the bank during 9M FY2020, the high slippages and muted cash recoveries/upgradations resulted in an increase in the gross NPAs to Rs. 8,923 crore (13.58%) as on December 31, 2019 from Rs. 8,606 crore (11.83%) as on March 31, 2019. As mentioned earlier, although P&SB received capital support from the GoI in 9M FY2020, its ability to improve the provision coverage on these loans remains low, given the weak capital cushions. The bank's provision coverage ratio (PCR%; including technical write-offs or TWOs) remained low at 62.1% as on December 31, 2019 (59.5% as on March 31, 2019) compared to the PSBs' average of 77.8% as on December 31, 2019. The PCR, excluding TWOs, was also low at 39.3%. Thus, with an increase in the gross NPAs, the net NPAs increased to Rs. 5,418 crore (8.71%) as on December 31, 2019 from Rs. 4,994 crore (7.22%) as on March 31, 2019.

With higher net NPAs and erosion in the core equity capital (because of losses), the bank's solvency profile deteriorated to 125.3% as on December 31, 2019 from 109.4% as on March 31, 2019. With a likelihood of losses in FY2021 as well, ICRA expects the solvency profile to remain weak.

Going forward, ICRA expects asset quality issues in the retail and MSME segment due to the adverse impact of Covid-19. Thus, assuming a slippage rate of 4.5-5.5% in FY2021 compared to 5.5-6.5% estimated for FY2020 and to bring the net NPA% below the PCA threshold of 6% by March 2021, ICRA expects the PCR to improve to 60-61% as of March 2021 and the credit provisions to remain at 1.6-1.8% of the average total assets (ATA) in FY2021 compared to 2.0-2.3% estimated for FY2020.

Weak operating profitability and low cover on stock of bad loans will further erode capital – P&SB's profitability remained weak in 9M FY2020 as well, with the reported loss before tax increasing to Rs. 1,134 crore (-1.44% of ATA) from a loss before tax of Rs. 859 crore (-0.78%) in FY2019. The higher loss before tax can be attributed to high credit costs with credit provisions of Rs. 1,625 crore (1.97% of ATA) in 9M FY2020, similar to Rs. 1,962 crore (1.78%) in FY2019. The credit costs continue to surpass the bank's operating profitability, which, in turn, has been weakening because of the declining loan book and high slippages (resulting in income reversals). P&SB's operating profitability, as a percentage of ATA, declined to 0.56% in 9M FY2020 from 0.94% in FY2019 and remains weaker than the PSBs' average of 1.53% for 9M FY2020 and 1.44% for FY2019.

Going forward, the credit provision estimates of 1.6-1.8% of ATA are expected to surpass the bank's core operating profitability, resulting in a negative RoA of 0.7-0.8% in FY2021 (compared to an estimated negative RoA of 1.0-1.2% in FY2020 and -1.4% in 9M FY2020).

Modest capitalisation profile and weak solvency; capital requirements in FY2021 remain sizeable – The bank's capitalisation profile remains modest with capital metrics i.e. CET I%, Tier I% and CRAR% of 7.61%, 9.37% and 12.04%, respectively, as on December 31, 2019, compared to 7.80%, 9.50% and 10.93%, respectively, as on March 31, 2019. Although the capital metrics remained above the minimum regulatory ratios[2], the capital cushions weakened on account of the sizeable losses before tax reported by the bank. Despite the large loss before tax of Rs. 1,134 crore in 9M FY2020, the erosion in the capital cushions was limited on account of a capital infusion of Rs. 787 crore by the GoI. Furthermore, given the reduction in the overall loan book (attributable to the decline in the corporate book), the RWAs moderated, partially cushioning the decline in the bank's core equity capital. P&SB also raised Rs. 100-crore equity capital by issuing shares to employees under the ESPS.

Going forward, assuming a degrowth of 2-4% in the RWAs in FY2021 and the earnings estimates mentioned earlier, ICRA expects P&SB to require capital of Rs. 1,500-2,000 crore (130-180% of the current market capitalisation) to maintain a cushion of 50 bps over the regulatory CET I% of 8.00% as on March 31, 2021. Considering the sizeable capital requirement, P&SB's dependence on the GoI for capital support would remain high as the bank has a limited track record of raising capital from the market over the last few fiscals. If the bank pursues credit growth, the capital requirement would increase, assuming the other factors remain the same.

Losses result in depletion of distributable reserves and weakening of serviceability of AT-I bonds – Given the losses reported in 9M FY2020, the bank's retained earnings or distributable reserves depleted during this period. As per the covenant for the AT-I bonds, in an event of a loss, the bank could service the coupon on the AT-I bonds though the distributable reserves created out of past profits, provided it meets the minimum regulatory capital ratios (including the CCB).

With the bank witnessing sustained losses in 9M FY2020, distributable reserves/RWAs declined to 2.5% as on December 31, 2019 from 3.1% as on March 31, 2019. Given the likelihood of losses in FY2021, distributable reserves/RWAs may decline further to 0.4-1.0% by March 31, 2021. A significant depletion in the distributable reserves would further weaken the coupon-servicing ability on the AT-I bonds and will remain a credit negative for the rating on the AT-I bonds.

Weak resource profile with low CASA share results in high cost of funds – P&SB's resource profile has traditionally been weaker than other PSBs, given the much lower share of current account savings account (CASA) deposits vis-à-vis the PSB average and greater reliance on high-cost bulk deposits. Supported by a modest YoY growth in CASA deposits and a YoY decline in overall deposits (because of a reduction in bulk term deposits), the CASA share improved to 27.7% as on December 31, 2019 from 26.8% as on March 31, 2019 and 24.5% as on December 31, 2018. Despite the improvement, the CASA share remained below the average PSB CASA share of ~39% as on December 31, 2019. With a low CASA share and greater reliance on bulk deposits, the bank's deposit concentration remains high, with the share of the top 20 depositors in overall deposits at 25.3% as on March 31,

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[2] *As per Basel III Capital Regulations (July 2015), a CCB of 2.5% was to be applicable from March 31, 2020. However, as per the new directives of the RBI on March 27, 2020, the CCB of 2.5% has been deferred to September 30, 2020. Thus, the regulatory CET, Tier I and CRAR as on March 31, 2020 were 7.375%, 8.875% and 10.875%, respectively, each of which would increase by 0.625% from September 30, 2020*

2019 against 26.2% as on March 31, 2018. This also remained above the average deposit concentration for PSBs. The cost of funds for P&SB remained high at 6.09% for 9M FY2020 and 6.08% for FY2019 compared to the PSB average of 5.03% for 9M FY2020 and 5.01% for FY2019.

Liquidity position: Strong

P&SB's liquidity profile remains strong despite reporting negative cumulative mismatches of 16.7% of the total outflows in the up to 1-year maturity bucket, as per its structural liquidity statement for December 2019. Given the higher reliance on bulk deposits (33% of total deposits and shorter tenor in nature), the bank has high outflows in the 6 months-1-year maturity bucket, resulting in moderate negative cumulative mismatches. The liquidity profile is, however, supported by a comfortable LCR of 176.78% (daily average for Q3 FY2020), which is well above the minimum regulatory requirement of 100%[3]. Moreover, P&SB has been holding excess SLR investments, which further aids its liquidity profile. As per ICRA's estimates, on a fortnightly average basis, P&SB's excess SLR holdings stood at 3.6% of the average net demand and time liabilities (NDTL) during August 2019-February 2020. Supported by its sovereign ownership and deposit franchise, ICRA expects P&SB to roll over its deposits upon maturity and maintain its liquidity profile.

Rating sensitivities

Positive triggers – Given the Negative outlook on the ratings at present, the ratings will not be upgraded. However, the rating outlook could be changed to Stable if the bank is able to reduce and maintain its net NPAs below 6% while improving its solvency (net NPA/core equity) to <65-70% on a sustained basis.

Negative triggers – ICRA could downgrade the ratings if the bank is unable to raise sufficient capital, resulting in a breach of the regulatory capital ratios (including the CCB). Continued losses, which would result in further depletion of the distributable reserves, would remain an additional trigger for the rating of the AT-I bond.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA Rating Methodology for Banks Impact of Parent or Group Support on an Issuer's Credit Rating ICRA Policy on Withdrawal and Suspension of Credit Rating
Parent/Group Support	The ratings factor in P&SB's sovereign ownership and the demonstrated track record of capital infusion by the GoI
Consolidation/Standalone	To arrive at the ratings, ICRA has considered the standalone financials of P&SB

[3] *On April 17, 2020, the RBI relaxed the regulatory LCR to 80%, with immediate effect, from 100% previously. The LCR will be restored to 100% by April 1, 2021 in a phased manner. The LCR would increase to 90% from October 1, 2020 and then to 100% from April 1, 2021*

About the company

Established in 1908, P&SB is a PSB with the GoI holding an equity stake of 83.06% in the bank as on December 31, 2019. As on that date, the bank had a well-established network of 1,521 branches and 1,047 ATMs. P&SB reported a loss after tax of Rs. 754 crore in 9M FY2020 against a loss after tax of Rs. 485 crore in 9M FY2019. Its asset quality indicators, i.e. GNPA% and NNPA% stood at 13.58% and 8.71%, respectively, as on December 31, 2019 compared to 11.19% and 6.90%, respectively, as on December 31, 2018. The capitalisation metrics, i.e., CRAR and Tier I stood at 12.04% and 9.37%, respectively, as on December 31, 2019 compared to 10.78% and 9.39%, respectively, as on December 31, 2018.

Key financial indicators (audited) – Punjab & Sind Bank

	FY2018	FY2019	9M FY2019	9M FY2020
Net interest income	2,235	2,280	1,850	1,553
Profit before tax	-595	-859	-829	-1,134
Profit after tax	-744	-543	-485	-754
Net advances	66,569	69,176	68,147	62,243
Total assets	1,12,912	108,052	109,337	102,123
% CET I	8.37%	7.80%	7.74%	7.61%
% Tier I	9.85%	9.50%	9.39%	9.37%
% CRAR	11.25%	10.93%	10.78%	12.04%
% Net interest margin	2.14%	2.06%	2.22%	1.97%
% PAT / ATA	-0.71%	-0.49%	-0.58%	-0.96%
% Return on net worth	-14.03%	-10.75%	-12.69%	-20.93%
% Gross NPAs	11.18%	11.83%	11.19%	13.58%
% Net NPAs	6.92%	7.22%	6.90%	8.71%
% Provision coverage excl. technical write-offs	40.94%	41.97%	41.23%	39.29%
% Net NPA/ CET	81.60%	109.35%	100.02%	125.27%

Note: Amount in Rs. crore; All calculations are as per ICRA research
Total assets and net worth exclude revaluation reserves
Source: P&SB, ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

S. No	Instrument	Type	Amount Rated	Amount Outstanding	Current Rating (FY2021)	Chronology of Rating History for the Past 3 Years				
					Date & Rating	Date & Rating in FY2020	Date & Rating in FY2019			Date & Rating in FY2018
					23-Apr-20	16-May-19	13-Mar-19	01-Jun-18	18-May-18	20-Apr-17
1	Basel III Compliant Additional Tier I	Long Term	1,000.00	1,000.00	[ICRA]A- (hyb) (Negative)	[ICRA]A+ (hyb) (Negative)	[ICRA]A+ (hyb) (Negative)	[ICRA]A+ (hyb) (Stable)	[ICRA]A+ (hyb) (Stable)	[ICRA]A+ (hyb) (stable)
2	Basel II Compliant Lower Tier II	Long Term	200.00	0.00	[ICRA]AA- (Negative); Withdrawn	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
			300.00	300.00	[ICRA]AA- (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
3	Certificates of Deposit	Short Term	10,000.00	10,000.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE608A09122	Tier II Bonds	11-Jan-2010	8.70%	11-Apr-2020	200.00	[ICRA]AA-(Negative); Withdrawn
INE608A09130	Tier II Bonds	24-Jun-2011	9.73%	24-Oct-2021	300.00	[ICRA]AA-(Negative)
INE608A08025	Additional Tier I	08-May-2017	10.90%	Perpetual*	1,000.00	[ICRA]A-(hyb)(Negative)
-	Certificates of Deposit	NA	NA	7-365 days	10,000.00	[ICRA]A1+

Source: Punjab & Sind Bank

**The instrument has a call option date of May 7, 2022*

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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

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