

Press Release for Andhra Bank's Issue Rating

Brickwork Ratings assigns "BWR AA+" for Andhra Bank's Tier I Perpetual Bonds Issue of INR 2.65 billion

Andhra Bank

Issue Rating: BWR AA+

Brickwork Ratings has assigned BWR AA+ (Pronounced BWR Double A plus) to Andhra Bank's proposed Tier I perpetual bonds issue INR 2.65 billion or Rs 265 crore. Brickwork Ratings has recently (dated) rated Andhra Bank's Perpetual Bond Issue with "BWR AA+" rating. Brickwork Ratings expects that this addition in the bank's perpetual bond issue will not change the ratings, since the bank remained well within its borrowing capacity and lending patterns. The rating factored majority ownership of the Government of India, favorable operating spread and returns, lower NPA, less risky loan portfolio, higher Tier 1 capital and leverage. However, the bank's operation largely concentrated in the state of Andhra Pradesh might be a limiting factor.

The Government of India (GoI) is a major shareholder of Andhra Bank with a stake of 51.55%. The bank is a mid sized public sector bank incorporated in 1923, was nationalized in 1980. The bank offers retail banking, small and medium enterprise (SME) banking, treasury and financial institutional services. The bank's total business increased 20.5% to reach INR 839.93 billion as on 31st March 2008. This high growth was sustained in spite of 23.55% growth recorded in the previous year - FY 2007. The bank's total deposits stood at Rs 494.36 billion, as on March 2008, a growth of 19.3% over 2007.

While Andhra Bank's total capital adequacy ratio increased to 11.61% in FY 2008, yet the ratio is less than that of its peers. The bank needs to supplement its capital. *Brickwork* calculates *Leverage* that assesses bank's capital adequacy with reference to both on balance and off balance sheet exposures. Andhra Bank has shown a reasonable leverage of 16.4 compared to its peer group at 21.3. In spite of lower leverage the bank's ROE was healthy at 17.97% in FY 2008. The bank is one of the profitable mid-sized public sector banks in India, with total income of INR 48.71 billion for FY 2008, reflecting the continued buoyancy in the bank's core business income, fee based income and focus on healthy asset-quality contributed to the improvement in the profitability. The non-interest income of the bank has been marginally lower than that of peers. To augment non-interest income, the bank continues to pursue multi channel approach to sell insurance and investment products. The efficient cash-management system coupled with higher income helped the bank improve its cost to income ratio to 47.2% from the previous of level of 50.1%.

The bank's lower cost CASA deposits declined to 33.6% and its credit deposit ratio has been higher than its peers. These imply that the bank may have to take liquidity enhancing measures. The bank's cost of mobilizing deposits increased from 5.32% to 6.58% during the year 2008. While the bank's net interest margin at 2.86%, is satisfactory compared to peers, yet the margin for Andhra Bank declined from the level of 3.20%. Further, the bank's total investment to total assets ratio stood at 26.33% as on 31st March 2008, on par with the peer group average. The bank's interest income from investments increased by 16.9% from INR 8.96 billion during 2006-07 to INR 10.48 billion in 2007-08 and during the period, the profit on sale of investments registered an increase of 121.9% with rupee profit of INR 1.19 billion. This is largely attributed to favorable market conditions and prudent portfolio management. In addition, the bank's yield on investments increased to 8.27% during 2007-08 from 7.34% in 2006-07.

BWR ratings on Andhra bank's perpetual bond issue by-and-large factored the Government of India ownership, quality of risk weighted assets, low cost deposit base, growth in income, decline in gross NPA, and lower leverage. The Bank is well placed to manage the key challenges in

liquidity, credit quality declines in the coming months. The bank's concentration in a single state as well as lower CASA deposits are limiting factors in the long run.

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