

---

## Rating Rationale for Corporation Bank's Upper Tier II Bonds Rating

---

### **Brickwork Ratings assigns “BWR AAA+” for Corporation Bank's Upper Tier II Bonds of INR 10 billion**

**Issue Rating: BWR AAA+**

**Outlook: Stable**

Brickwork Ratings has assigned BWR AAA+ (Pronounced BWR Triple A Plus) for Corporation Bank's proposed Upper Tier II Capital Bonds issue of INR 1000 crore or INR 10 billion. Brickwork Ratings' 'BWR AAA+' stands for an instrument that is considered to offer the BEST credit quality in terms of timely serving of debt obligations. The rating factored higher operating profits, improving asset quality, comfortable capital adequacy, healthy low cost deposits, stable earning assets, well diversified credit deployment, optimum operating cost structure and the Government of India's equity stake.

BWR has essentially relied upon audited financial statements of FY ending March 2008 and has also considered the quarterly performance reported by the Bank up to 31<sup>st</sup> December 2008 based on limited review and information and clarification sought by us and provided by the Bank.

The Bank has posted strong growth in total business, deposits and advances along with continuously improving quality of loans during FY 08. With total business growth of 30.85%, the Bank skillfully prevailed over the challenging economic conditions during FY 08, and has grown further by 27.74% till Q3 FY 09.

The Bank's asset quality is the best among its peer group. During FY08, the Bank's gross NPAs stood at 1.47%, which is 56 bps lower than that of peers' 2.03%. Similarly, the net NPAs at 0.32%, was 60 bps lower than the peers' average of 0.92%. During Q3 FY 09, the asset quality has improved even further, where the gross NPAs declined to 1.24% (1.71% in Q3 FY 08).

The Bank has generated impressive revenues and profit figures with significant improvement in core income and fee based income. As a result, the Bank's profit before

tax and net profit surged 30.47% (INR 10.65 billion) and 37.09% (INR 7.34 billion) respectively during FY 08.

**Table I: Corporation Bank's Improving Strengths**

Criteria	FY 07	FY 08	Q3 FY 09
<b>Deposits (INR Billion)</b>	423.56	554.24	618.94
<b>Demand and Saving Deposits</b>	144.29	194.05	156.08
<b>Term Deposits</b>	279.28	360.19	462.85
<b>Advances (INR Billion)</b>	299.49	391.85	449.37
<b>Non-Performing Assets</b>			
<b>Gross NPAs</b>	2.05%	1.47%	1.24%
<b>Net NPAs</b>	0.47%	0.32%	0.33
<b>Profit</b>			
<b>Gross Profit (INR Billion)</b>	11.40	12.51	4.49
<b>Net Profit (INR Billion)</b>	5.36	7.34	2.56
<b>ROA</b>	1.11%	1.38%	1.46%
<b>ROE</b>	14.24%	17.38%	17.34%
<b>Business per Employee (INR Billion)</b>	0.064	0.083	0.092
<b>Net worth (INR Billion)</b>	37.65	42.29	48.61
<b>CRAR</b>	12.76%	12.09%	12.76%
<b>Branches</b>	901	981	1036
<b>ATMs</b>	929	957	1023

The strategy of emphasizing on clientele base expansion and thrust on increasing the share of core deposit in the overall deposit mix of the Bank, adopted in previous year, was continued during FY 08. As a result, the Bank's **total deposits** have registered a net addition of INR 130.67 billion to reach INR 554.24 billion during FY08, registering a growth of 30.85% during the year, which have grown further during Q3FY 09 to reach INR 618.94 billion. Demand deposits in the total deposit mix increased from 34.07% to 35.01% for the year 2007-08. In absolute terms, the demand deposits grew from INR 144.29 billion to INR 194.05 billion during FY 08 registering a growth rate of 34.49% during the year. The Bank's savings deposits portfolio registered a growth rate of 16.30% to close at INR 89.99 billion during FY 08. More over, the Bank's current deposits also improved to INR 105.06 billion during FY08 recording a growth rate of 55.02%. Similarly, the term deposits have increased by INR 80.91 billion and stood at INR 360.19

---

during FY 08 registering growth of 28.97% and have grown further in Q3 FY 09 to reach INR 462.85 billion.

The **credit portfolio** of the Bank registered a robust growth of 30.84% during FY 08. Growth in the credit was achieved through intense marketing of the various loan products of the Bank both under retail and corporate segments. Advances increased from INR 299.50 billion as on 31<sup>st</sup> March 2007 to INR 391.86 billion as on 31<sup>st</sup> March 2008, thus registering an absolute increase of INR 92.36 billion. The Bank has increased its gross advances during Q3 FY 09 to reach a level of INR 449.37 billion. Retail lending continued to be a focus area. The outstanding credit under retail lending improved from INR 76.61 billion during FY 07 to INR 88.13 billion during FY 08, registering a growth of INR 11.51 billion. The Bank has set up 18 retail hubs and 2 retail and agricultural hubs exclusively for quick delivery of retail and agricultural loans.

The Bank has maintained high standard in **asset quality** through appropriate risk management measures and recovery measures as evidenced by lower NPA levels. Close surveillance and initiation of prompt remedial action in borrowal accounts has ensured high quality of assets for the Bank. It is evidenced by the fact that the standard assets constitute 98.53% of the Bank credit as on 31<sup>st</sup> March 2008. Over the years, the Bank's asset quality has been steadily improving through better credit culture and monitoring. As a result, Gross NPAs have come down to 1.47% as on 31<sup>st</sup> March 2008 from 2.05% for the same period a year ago. The Bank's Net NPAs have shown a similar trend, which have declined to 0.32% in FY08 from 0.47% in FY07. The declining trend in the non-performing assets has been witnessed not only in the percentage terms, but also in absolute level. The Bank's gross NPAs stood at INR 5.84 billion during FY08 as compared to INR 6.24 billion during FY07.

Interest income recorded a growth of INR 11.56 billion from INR 33.60 billion in the year 2006-07 to INR 45.16 billion during the year 2007-08 as against the interest expenses which grew from INR 20.52 billion during FY 07 to INR 30.73 billion during FY 08. The Bank's net interest income recorded a growth of INR 1.35 billion during the same period. Similarly, non-interest income increased by INR 0.64 billion from INR 6.35 billion in FY 07 to INR 6.99 billion in FY 08. The Bank has posted strong quarterly gross profit of INR 4.49 billion for the third quarter ended December 31, 2008 up 61.90% Q-o-Q. Further, the Bank posted 34.30% growth in **net profit** to reach INR 2.56 billion in Q3 FY 09, as compared to INR 1.90 billion for the same period a year ago. The interest

income on advances continued to be a major contributor to the Bank's top line performance with a 45.80% growth and equally well supported by fee income with 39.91% growth. As on 31<sup>st</sup> December 2008, the Bank has provided its loan loss coverage of 73.24%.

The Bank has an internal capital adequacy assessment policy to comprehensively evaluate capital adequacy requirements. The Bank had a **capital adequacy ratio** of 12.09% as on 31<sup>st</sup> March 2008, which is well above the minimum stipulated 9%. Keeping in view the growth, the Bank has identified capital requirements for the year. Accordingly, the Bank has issued Tier II Subordinated Bonds of INR 5.00 billion in Q3 FY 09, due to which the capital adequacy ratio improved significantly to 12.76% by December 2008. It is expected that the proposed issue of INR 10 billion would further improve the CRAR.

During FY 08, the Bank's **Net Worth** had improved progressively to reach INR 42.29 billion with 12.32% growth over the previous year. Similarly, the Bank's **Return on Assets** stood at 1.38% during FY 08, which is 12 bps higher than that the previous year figure of 1.26%. **ROE** has also improved consistently from 14.24% in FY 07 to 17.38% end of FY 08.

The Bank's aggregate investment as on 31<sup>st</sup> March 2008 stood at INR 173.89 billion with maturity mix of securities consistent with the risk perceptions and investment policy guidelines. Treasury operations have been yielding significant returns. During FY08, the Bank has generated INR 1.35 billion income from treasury operations, with a growth rate of 7.14% and yield of 7.37%. Despite difficult market conditions, yield on investments have improved to 7.70% as on 31<sup>st</sup> December 2008.

**Table II: Corporation Bank Vs Peer Group**

<b>Key Ratios</b>	<b>CORP</b>	<b>Peers</b>
<b>Operating Ratios</b>		
Cost of Deposits	6.45%	6.28%
Cost of Borrowings	3.73%	4.56%
Cost of Funds	5.76%	6.11%
Return on Funds	8.47%	8.98%
Net Interest Margin	2.71%	2.77%

<b>Profitability</b>		
Return on Assets (ROA)	1.38%	1.16%
Return on Equity (ROE)	17.38%	20.92%
<b>Asset Quality (As % of Advances)</b>		
Gross NPA	1.47%	2.03%
Net NPA	0.32%	0.92%
Real Estate Loans	17.41%	9.51%
Term Loans	54.72%	57.13%
<b>Capital Adequacy</b>		
Tier 1	9.64%	8.26%
Total Capital	12.09%	11.79%
Leverage	15.1	20.7
<b>Liquidity</b>		
CASA	35.01%	31.10%
Credit Deposit Ratio	70.70%	69.42%

BWR has made a study of the performance of Corporation Bank vis-à-vis its peers in certain key parameters as given in the table above. BWR rating methodology has defined peer banks as those with closely similar size/operation as the Corporation Bank.

It is observed that the Bank has got the lowest cost of borrowings and cost of funds among its peers as on 31<sup>st</sup> March 2008. The Bank's cost of deposits is however comparatively higher which has dipped the net interest margin slightly as compared to its peers.

The Bank's return on assets at 1.38% is the highest amongst similar sized banks, though ROE is comparatively lower. The Bank stands out as the best performer as regards quality of advances. The gross and net NPAs are substantially lower at 1.47% and 0.32% respectively as against the peers' 2.03% and 0.92% respectively.

The Bank's term loan component at 54.72% against peers' figure of 57.13%, works to the Bank's advantage.

Amongst the peer banks, as on 31<sup>st</sup> March 2008, the Corporation Bank's CASA deposit ratio at about 35% is the highest. Although this ratio slipped subsequent to 31<sup>st</sup> March

---

2008, it is observed that consistent efforts are being made to increase the low cost deposits and improve the ratios.

Corporation Bank has the **highest capital adequacy ratio** amongst its peers. As of 31<sup>st</sup> March 2008, the CRAR was 12.09%, which has significantly improved to **12.76%** by end of December 2008. The CRAR is expected to improve further with the proposed issue of upper Tier II capital issue of INR 10.00 billion.

A special feature of BWR, it is an application of leverage ratio for analyzing the Bank's performance. Brickwork calculates Leverage that assesses Bank's capital adequacy with reference to both on and off balance sheet exposures. The Bank has shown the best leverage of 15.1 as compared to its peers' average of 20.7.

**Overall, it is found that Corporation Bank's performances on most of the parameters are superior to that of its peers.**

#### Shortcomings:

In the analysis of the Corporation Bank's performance for FY 2008 and the subsequent period, April–December 2008, a few shortcomings as under have been noticed.

- a) The share of CASA deposits has slipped from 35.01% as of March 2008 to about 25.22% by third quarter ending December 2008.
- b) Consequently the cost of deposits has increased from 5.3% in FY07 to 6.45% in FY08 to 6.91% in Q3 FY09.
- c) The net interest margin declined from 3.08% in FY07 to 2.71% in FY08 to 2.53% in Q3 FY09.
- d) The real estate exposure at 17.41% of the total advances as at FY08 is high compared with the peers, though it has come down from 22.24% in FY 07.
- e) The capital market exposure of the Bank has also shown an increase from 0.53% of the total advances in FY07 to 2.15% in FY08.

#### Mitigants:

The Bank has been conscious of the aforesaid deficiencies and is taking requisite steps to bring about improvements. The Bank is making concerted efforts to reduce its

dependence on high cost bulk deposits. It has introduced several new schemes for mobilizing new savings deposits and is actively pursuing them through appropriate marketing strategies to improve the low cost CASA deposits. It is also en-cashing upon its technology initiative, especially the cash management services where the Bank is still a dominant player, the total adoption of CBS in all its branches, the faster mode of remittances of funds through the recently introduced RTGS / ETF facilities to augment its current account deposits. The Bank has got a well-spread of branches in metro / urban, semi-urban and rural areas in the 5 states of Southern India. About 422 branches are located in semi-urban and rural areas which offer great scope for improving the low cost deposits. The Bank is taking adequate steps to tap the potential and expand banking services in such areas not only through the help of the branches but also with the additional delivery channels like the ATMs and the bank correspondents. It has strengthened its sales and marketing infrastructure to ensure steady clientele acquisition and also for cross selling and up-selling of various products introduced by the Bank. Overall the Bank is taking necessary steps for overcoming the deficiencies.

In respect of the exposure to real estate sector, the exposure which was 22.24% in FY07 has come down to 17.41% in FY08 due to concerted efforts and it is expected that the declining trend will continue. Of this, the exposure to commercial real estate is just about 6.10%. The remaining portion of advances is for financing residential houses.

Similarly as regards the capital market exposure, the major increase was to meet the Bank's commitments towards venture capital and partly for margin trading. As we understand these are adequately secured. As part of its strict compliance with the risk management processes in the Bank, these exposures are expected to be handled carefully depending upon the market circumstances. The exposures in the above sectors, being a small portion of the total advances is unlikely to have any major impact.

#### **Management of Risk:**

The Bank has an adequate risk management system in place duly approved by the Bank's board to take care of credit, market, and operational risks. The board periodically reviews the same. Accordingly it has put in place an appropriate machinery to identify measure, monitor and control the overall level of risks undertaken.

---

## Other Important Features:

### Overseas Representative Offices

During FY 09, the Bank had opened representative offices at Dubai and Hong Kong for exploring business opportunities.

### Domestic Expansion

The Bank has put in place 20 retail hubs covering 639 link branches during FY 09 to facilitate the prompt disbursement of retail loans. Further, the Bank has taken initiative to install 25 transaction KIOSKS and the first KIOSKS has been installed in M G Road, Mangalore.

### New Products Launched

The Bank has launched Corp New Gen savings bank account targeted at students with lower quarterly average balance requirements and various concessions in charges and other value added facilities. Further, the Bank has launched its own credit card in association with VISA International for the customers of the Bank.

The Corporation Bank is the first PSB to launch online educational loans. Further it provides an umbrella of financial services to retail investors using the Bank's alliance in adjacent markets such as life, non-life, and health insurance, mutual funds, gold banking, etc.

### Rating Outlook:

Incorporated in 1906, Corporation Bank is one of the oldest mid-sized public sector banks in India. The Bank has always been in the forefront to improve its productivity and efficiency. Over the years the Bank has been transforming itself from core banking activities to universal banking solutions.

The Bank has positioned itself very well in the southern part of the country. As a result, the Bank was able to show relatively good deposit growth compared to its peers in India. The Bank continues to expand its technology driven customer-centric products and services to serve effectively its growing customer base. The Bank's product and services consist of cash management services, money market related products, treasury asset

managements, forex services, payments and receipts, remittance, merchant banking LIC premiums, SME banking facility etc. During FY 08, the Bank has added 0.27 million customers to reach 1.0 million customers. The Bank has implemented Core Banking Solution (CBS) in all its branches, thus covering 100% of overall business. The Bank has put in pioneering efforts by launching branchless banking project. Under this project, the Bank used modern, yet cost effective ICT technologies and services of business correspondents such that the customer in rural areas can conduct simple transactions related to savings and loans without visiting the Bank's branch. These are 105 such locations functioning spread over all the 5 southern states.

Brickwork Ratings (BWR) issue rating is based on CAMEL-TP framework, which is used to assess the Bank's financial fundamentals and risk exposures. Brickwork Ratings has assigned BWR AAA+ to Corporation Bank is specific to the proposed Upper Tier II bonds issue of INR 1000 crore or INR 10.00 billion. The rating has factored majority stake held by Government of India, lean operating structure, well diversified loan portfolio and income stream, and comfortable capital adequacy ratios and all other related significant features discussed above.

The Bank's strong growth in advances and deposits, decline in NPAs, comfortable capital adequacy ratio, adequate risk management systems, and the healthy earning assets are expected to help the Bank to manage the current economic situation.

Copyright ©, 2009, Brickwork Ratings.

Brickwork Ratings (BWR) has assigned the rating based on the information obtained from issuer and other reliable sources, which are deemed to be accurate. BWR has taken considerable steps to avoid any data distortion; however, it does not examine the precision or completeness of the information obtained. And hence, the information in this report is presented "as is" without any express or implied warranty of any kind. BWR does not make any representation in respect to the truth or accuracy of any such information. The rating assigned by BWR should be treated as an opinion rather than a recommendation to buy, sell or hold the rated instrument and BWR shall not be liable for any losses incurred by users from any use of this report or its contents. BWR ratings are subject to a process of surveillance which may lead to revision in ratings. BWR has the right to change, suspend or withdraw the ratings at any time for any reasons.

## Analysts

**A. Suresh Kumar,**

suresh.kumar@brickworkratings.com

**Praveen**

praveen.prakash@brickworkratings.com

## Media

**Anitha G**

media@brickworkratings.com

## Relationship

K.N. Suvarna

Sr. V.P - Business Development

kn.suvarna@brickworkratings

Brickwork Ratings (BWR) has adopted SEBI's standardized Rating Symbols and their definition advised vide SEBI circular CIR/MIRSD/4/2011 dated June 15,2011, with effect from June 21, 2011. While there is no change in the Rating symbol as a consequence to the above, for the amended definition of the Rating, please refer to <http://www.brickworkratings.com/scale.html>. It is clarified that the said change in the definition should not be construed as a change in the Rating.