Press Release

UCO Bank

November 11, 2020

Rating Reaffirmed

Total facilities Rated*	**Rs.1000.00 Cr.**
Long Term Rating	ACUITE AA-/Stable (Reaffirmed)

* Refer Annexure for details

Rating Rationale

Acuité has reaffirmed the long-term rating of '**ACUITE AA-' (read as ACUITE double A minus)** on the Rs.1000.00 crore Non-Convertible Basel III Compliant Tier-2 Bonds of UCO Bank. The outlook is **'Stable'**.

About UCO Bank:

Kolkata based, UCO Bank was founded in 1943 by the industrialist Mr. G. D. Birla as United Commercial Bank. The bank was nationalised in 1969 and renamed as UCO Bank in 1985. UCO Bank is a public sector bank which is engaged in retail banking, corporate/Wholesale banking, priority sector banking, treasury operations and other banking services. The bank operates through a network of 3087 branches in India and 2 overseas branches, one each in Hong Kong and Singapore. The bank also has 2281 ATMs as on September 30, 2020.

UCO Bank was listed on BSE and NSE in 2003. The Government of India holds 94.4 percent stake in the bank as on September 30, 2020.

Analytical Approach

Acuité has adopted the standalone approach to analyse the business and financial profile of UCO Bank. The ownership and the ongoing support from the Government of India is central to the rating.

Key Rating Drivers

Strengths

- **Government of India ownership with track record of support:**

UCO Bank, headquartered in Kolkata, is among the 14 banks nationalised in 1969. The Government of India (GoI) holds 94.4 percent stake in UCO Bank as on September 30, 2020 (92.5 percent as on September 30, 2019), which is one of its largest shareholdings in any public sector bank. The bank has a pan-India presence through a network of 3087 branches of which 35 percent branches are in the eastern region of India and the balance are spread across other regions. UCO Bank has a moderate international presence with 2 overseas branches, one each in Hong Kong and Singapore. The bank plays a vital role in supporting the financial inclusion initiatives of the Government in the east and the north-eastern regions.

The GoI has been proactively supporting the Public sector Banks through a regular infusion of funds in order to ensure their financial health, necessary for discharging their role as catalysts of economic growth and financial inclusion. The GoI had recently announced mergers amongst the various public sector banks as a consolidation measure. As a part of this initiative, most of the relatively weak banks are being merged with the stronger PSU Banks based on criteria such as geographical orientation, technology platform commonality etc. UCO Bank, despite being under PCA framework, has been able to retain its independent identity as the Government has kept the bank outside the scope of these mega-mergers. This indicates the regional importance of UCO Bank.

Over the past 4 years, 11 PSU banks (including UCO Bank) were placed within the purview of Prompt Corrective Action Framework (PCA) by RBI on account of the continued deterioration in their key operating metrics such as Capital Adequacy, Profitability and Asset Quality. UCO Bank was included in the PCA framework in May 2017. Government of India allocated Rs. 88,139 Cr. during FY2018 as a part of its recapitalisation initiative to strengthen the weakening capital position of these PSU banks. Government has infused Rs. 20,045 Cr. Cr. in UCO Bank from FY2016 till FY2020, indicating the strategic importance of UCO Bank to GoI and the role it continues to play particularly in the economy of the eastern part of India.

The ongoing support from GoI has helped UCO Bank in maintaining its overall Capital Adequacy stood at 11.80% as on September 30, 2020 as against the required benchmark level 10.875 percent. Capital Adequacy levels stood at 11.70% as on March 31, 2020 and 10.70% as on March 31, 2019. The tier-I equity capital stood at 8.99% as on September 30, 2020. Presently the bank continues to remain under PCA, however, has shown signs of a turnaround in terms of meeting capital adequacy and profitability.
Acuite believes that GoI will continue to support UCO Bank in its revival path through further capital infusion, as and when required for adherence to the regulatory benchmarks. The continued ownership of GoI coupled with timing and magnitude of support will, nevertheless, be the key monitorables.

- **Healthy retail deposit franchise in its area of operations:**

UCO Bank has a pan India presence with around 35 percent of its branches (as on September 30, 2020) in the eastern states, followed by 20 percent branches in north India and the balance distributed across Western and Southern regions. UCO Bank has 61 percent of its branches in the rural and semi-urban regions which facilitates the mobilisation of small ticket deposits. Retail deposits account for ~49% of the total deposits as on March 31, 2020 On the strength of the extensive branch network, the retail deposits increased to ~ Rs. 96,147 Cr. as on June 30, 2020 from ~Rs. 89,693 thousand Cr. as on March 31, 2019.

The bank has benefitted from a strong Current Account Saving Account (CASA) base, which accounted for 39.18 percent of the total domestic deposits as on March 31, 2020 (previous year- 43 percent). This compares favourably with its peers among mid-sized public sector banks. Further, the increasing share of retail deposits in the overall deposit base reflects the strong retail franchise in its key operating regions. Since retail deposits are more stable than bulk deposits, the contribution from the retail deposit segment augurs well from the stability standpoint.

In addition to the strong retail deposit platform, UCO Bank also benefits from being nominated for routing of trade transactions under 'Rupee Payment Mechanism' between India and Iran. In view of the US sanctions against Iran, India's imports of crude from Iran are required to be settled in Indian Rupees. As per this arrangement, the oil importing companies deposit their payments for crude oil imports in the Rupee Accounts maintained with UCO Bank. Similarly, any exporter from India to Iran will receive payments for the exports from these accounts. Since India's trade balances with Iran are usually in a deficit, UCO Bank stands to benefit considerably by way of large balances in these accounts which are profitably deployed in the various liquid investment options such as interbank markets, among others. These balances, however, are volatile depending on the magnitude of transactions with Iran. The balance as on June 30, 2020 was Rs. 3176 Crs as against Rs. 18,387 Cr. as on March 31, 2019 due to moderation in the transactions.

Acuite expects UCO Bank to benefit by way of a lower cost of funds on the back of its stable retail deposit base and large current account balances accruing from the Iranian trade account.

Weakness:

- **Sustainability of improvement in key operating parameters to be demonstrated:**

The bank was placed under prompt corrective action (PCA) in May 2017 mainly on account of deterioration in its key parameters such as asset quality, Return on Average Assets (RoAA) and capital adequacy. Gross Non-Performing Assets (GNPAs) levels had increased from Rs. 6,621 Cr. as on March 31, 2014 to a peak of Rs. 30,549 Cr. as on March 31, 2018, mainly on account of increased delinquencies in key sectors such as Power and Steel sector to which UCO Bank has significant exposure. The elevated credit costs resulted in deterioration of profitability and the bank posted Net losses for the period FY2018-FY2020. Net loss stood at Rs. 4436 Cr. for FY2018, Rs. 4321 Cr. for FY2019 and Rs. 2437 Cr. for FY2020. The impact of these losses on capital adequacy levels was significantly mitigated by continuous infusion by GoI (~Rs. 17185 Cr. between FY2018 to FY2020).
Restrictions on lending, under the PCA framework, has resulted in moderation of incremental slippages. Incremental slippages stood at Rs. 15,034 Cr in FY2018, Rs. 9082 Cr. for FY2019 and further declined to Rs. 6181 Cr. for FY2020. Since then, GNPA levels have declined to Rs. 19,282 Cr. as on March 31, 2020. Consequently, provisions and write-offs have declined from Rs. 7520 Cr for FY2018 and Rs. 8495 Cr in FY2019 to Rs. 6477 Cr for FY2020.
The gross NPA levels have now declined to Rs. 13,366 Cr. as on September 30, 2020. i.e. 11.62 percent of total advances as on September 30, 2020. Provisioning coverage ratio (including TWO) stands at 89% as on September 30, 2020 and NNPA ratio has improved to 3.63 percent as on September 30, 2020 as against 13.1%

as on March 31, 2019 and 9.72% as on March 31, 2019. The Net NPA to net worth ratio as on September 30, 2020 stood at 20 percent (55 percent as on March 31, 2019). However, it is pertinent to mention that, presently the Supreme Court has restricted banks and financial institutions from classifying accounts as NPA and banks and financial institutions have to maintain status-quo on the accounts as on 31st August, 2020, hence the position of slippages will be understood only after the regulatory stance in this regard has emerged.
The bank has shown initial signs of turnaround over the past three quarters, i.e. since March 2020, registering profits and decline in GNPA levels. The bank posted net profit of Rs. 17 Cr. for 4QFY20, Rs 21 Cr. for Q1FY2021 and Rs.30 Cr. for Q2FY2021. The improvement in profitability was mainly contributed by Increase in Treasury income (supported by the declining trend of yields) (Rs.451 Cr, Rs. 651 Cr., Rs. 307 Cr in Q2FY21, Q1FY21 and Q4FY20 respectively) and recoveries from technically write off accounts (Rs.96 Cr, Rs.28 Cr. and Rs. 237 Cr. in Q2FY21, Q1FY21 and Q4FY20respectively). Till the performance of credit book supports the overall profitability, UCO bank will have to depend on treasury gains and recoveries. The bank's ability to maintain the momentum of treasury gains and recoveries in its write-off accounts is crucial to sustain the improvement in profitability.
The ability of the bank to sustain the improvement in key parameters and profitability amidst the current challenging environment will be critical to the maintenance of a stable credit profile.

Rating Sensitivity:
- Ownership of GoI and continuing support by way of equity infusion
- Improvement in capital adequacy levels
- Significant movement in asset quality and profitability parameters
- Exit from PCA framework

Material Covenants: None

Liquidity Position: Adequate
UCO Bank has adequate liquidity position as reflected in healthy Liquidity Coverage Ratio (LCR) of 187.5% percent as on March 31, 2020 as against the regulatory requirement of minimum 100 percent. In terms of funding profile, UCO Bank has a Net stable funding ratio of 166.83 percent as on March 31, 2020. Besides maintaining CRR and SLR in excess of statutory requirements, the bank has also maintained liquid investments in non-SLR category which provide liquidity buffers.

Outlook: Stable
Acuite believes that UCO Bank will maintain a 'Stable' outlook on the back of continuing support from the Government of India and its important position in the public sector banking system. The outlook may be revised to 'Positive' in case UCO Bank is able to demonstrate a significant and sustainable improvement in profitability, asset quality and capital adequacy. The outlook may be revised to 'Negative' In case the bank faces challenges in attaining a significant improvement in asset quality, profitability and capital adequacy parameters.

About the Rated Entity - Key Financials

Parameters	Unit	FY20 (Actual)	FY19 (Actual)
Interest Income	Rs. Cr.	15134.33	14330.63
Interest Expense	Rs. Cr.	10042.06	10019.48
Profit After Tax (PAT)	Rs. Cr.	(2436.83)	(4321.09)
Deposits	Rs. Cr.	193203.44	197906.78
Net Advances	Rs. Cr.	101174.25	99313.84
Investments	Rs. Cr.	90998.81	82231.69
Capital Adequacy	(%)	11.70	10.70
Return on Average Assets (RoAA)	(%)	(1.09)	(2.00)
Gross NPA	(%)	16.77	25.00
Net NPA	(%)	5.45	9.72

Status of non-cooperation with previous CRA (if applicable)
None

Any other information
None

Applicable Criteria

- Banks And Financial Institutions - https://www.acuite.in/view-rating-criteria-45.htm
- Default Recognition - https://www.acuite.in/view-rating-criteria-52.htm
- Financial Ratios And Adjustments - https://www.acuite.in/view-rating-criteria-53.htm

Note on complexity levels of the rated instrument
https://www.acuite.in/view-rating-criteria-55.htm

Rating History (Upto last three years)

Date	Name of Instrument/ Facilities	Term	Amount (Rs. Cr)	Ratings/Outlook
08 Nov, 2019	Non-Convertible Basel III Compliant Tier-2 Bonds	Long Term	500.00	ACUITE AA-/Stable (Assigned)
	Non-Convertible Basel III Compliant Tier-2 Bonds	Long Term	500.00	ACUITE AA-/Stable (Reaffirmed)
18 April, 2019	Proposed Non-Convertible Basel III Compliant Tier-2 Bonds	Long Term	500.00	ACUITE AA-/Stable (Assigned)

***Annexure – Details of instruments rated**

ISIN	Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
INE691A08062	Non-Convertible Basel III Compliant Tier-2 Bonds	16-12-2019	9.71%	16.12.2029	500.00	ACUITE AA-/Stable (Reaffirmed)
INE691A08054	Non-Convertible Basel III Compliant Tier-2 Bonds	28-06-2019	9.64%	28.06.2029	500.00	ACUITE AA-/Stable (Reaffirmed)

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About Acuité Ratings & Research:
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