August 17, 2022

Small Industries Development Bank of India: [ICRA]AAA (Stable) assigned to long-term bonds programme; rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term bonds programme	-	20,000	[ICRA]AAA (Stable); assigned
Long-term bonds programme	18,635	18,635	[ICRA]AAA (Stable); reaffirmed
Long-term bonds programme	1,365	-	[ICRA]AAA (Stable); reaffirmed and withdrawn
Total	**20,000**	**38,635**	

**Instrument details are provided in Annexure I*

Rationale

The rating for Small Industries Development Bank of India (SIDBI) factors in its position as an apex financial institution (FI) for the promotion and development of the micro, small and medium enterprise (MSME) sector in India. SIDBI was established under an Act of Parliament in 1990 and is jointly owned by the Government of India (GoI; 20.85%), public sector banks (PSBs), insurance companies and other FIs as on March 31, 2022.

To enhance SIDBI's competitive funding position, the GoI facilitates access to low-cost micro and small enterprise (MSE) funds[1] for onward refinancing to eligible lending institutions at competitive rates. The allocation for FY2023 stood at Rs. 65,000 crore, which was higher than the allocation for previous years, and is available at a concessional interest rate. These MSE funds accounted for 61% of SIDBI's total borrowings as on March 31, 2022 and supported the competitive cost of funds for the bank.

As a part of its lending operations and refinancing activities, SIDBI takes exposure to scheduled commercial banks (SCBs), private entities other than banks, and non-banking financial companies (NBFCs). Some of the counterparties, especially in the direct lending segment could be weak, while a few lumpy NBFC exposures have also slipped in recent years resulting in a relative increase in the overall slippages during such years. However, SIDBI has largely provided for these exposures and the headline asset quality metrics remain strong with the net non-performing advances (NPAs) at 0.06% as on June 30, 2022 (0.07% as on March 31, 2022 and 0.12% as on March 31, 2021).

Further, SIDBI's leverage[2] stood at 8.81 times as on March 31, 2022 (7.91 times as on March 31, 2021), which is well within the regulatory permissible levels. However, its borrowings are likely to increase with the targeted credit growth for FY2023 and the leverage is expected to rise, although it is expected to remain with the allowed limits. SIDBI's capitalisation levels remain comfortable with a capital-to-risk weighted assets ratio (CRAR) of 21.53% as on June 30, 2022 (24.28% as on March 31, 2022 and 27.49% as on March 31, 2021), which, in turn, is supported by the lower risk weights for the refinance book. SIDBI has a superior liquidity profile with positive asset-liability gaps in the short as well as long term, which are supported by the matching tenure of the assets (refinancing loan book) and the liabilities (MSE funds). The liquidity profile is further supported by standby lines from banks, including the pending drawdown against the allocated MSE fund.

ICRA expects that SIDBI will continue to benefit from its role of an apex FI for the development of the MSME sector and its strategic importance to the GoI, driving the Stable outlook on the rating. Given the cap on lending margins, the earnings

[1] MSE fund is created out of deposits from SCBs against their shortfall in priority sector lending (PSL) targets

[2] Leverage = Total debt/Net owned funds; As per Reserve Bank of India (RBI) regulations, All India Financial Institutions (AIFIs) have to maintain a leverage of 10 times, though SIDBI has received approval for a higher leverage of 14 times till March 31, 2023

profile in terms of return on assets/equity (RoA/RoE) is likely to remain modest, though the profitability is likely to be sufficient for achieving the targeted growth without fresh equity capital requirements in the near to medium term.

ICRA has withdrawn the rating assigned to the Rs. 1,365.00 crore long-term bonds as they have matured. The rating was withdrawn in accordance with ICRA's policy on withdrawal and suspension (ICRA Policy on Withdrawal).

Key rating drivers and their description

Credit strengths

Strategic importance to GoI for development of MSME sector – SIDBI is an FI established in 1990 under an Act of Parliament (SIDBI Act, 1989). Under the Act, SIDBI has been described as a development bank established as 'the principal financial institution for the promotion, financing and development of industry in the small-scale sector and to coordinate the functions of the institutions engaged in the promotion, financing or developing of industry in the small-scale sector and for matters connected therewith or incidental thereto'.

Further, Tier I capital bonds amounting to Rs. 1,423 crore were converted into equity share capital in FY2022, resulting in an increase in the GoI's share to 20.85% as on March 31, 2022 from 15.40%. Besides this, State Bank of India (SBI), which has the second highest shareholding in SIDBI, had a stake of 15.65% following the conversion (16.73% as on March 31, 2021) while the share of Life Insurance Corporation of India (LIC) stood at 13.33% as on March 31, 2022 (14.25% as on March 31, 2021). The rest is held by other PSBs and institutions.

ICRA, however, notes that despite the relative increase in the GoI's stake, the overall shareholding remains fragmented. Hence, in the absence of a single dominant shareholder or promoter, future capital raising, if any, will remain dependent on the ability and willingness of all the shareholders to contribute capital in a timely manner. Nevertheless, given the current capitalisation levels, the requirement for capital support remains limited in the near to medium term.

Capitalisation metrics remain comfortable– As the overall systemic liquidity narrows, demand for refinance is expected to increase. SIDBI plans to grow its total assets by ~30% in FY2023 against which the Reserve Bank of India (RBI) has allowed it to borrow up to a leverage of 14 times till March 31, 2023 to meet the increasing refinancing requirements. Against this, SIDBI's leverage remains comfortable at 8.81 times as on March 31, 2022 (7.91 times as on March 31, 2021).

SIDBI's exposure to various banks attracts a low-risk weight of 20%, resulting in strong capital adequacy levels with a CRAR of 21.53% as on June 30, 2022, although the same moderated from 24.28% (entirely Tier I) as on March 31, 2022 (27.49% as on March 31, 2021). ICRA notes that while the implementation of Basel III for AIFIs is yet to be announced, an eventual change in the method of computing risk-weighted assets upon the adoption of Basel III will not impact the capital metrics materially. Therefore, the overall capitalisation profile is expected to remain strong.

Strong asset quality indicators – SIDBI's refinance portfolio accounted for 92.90% of the total net advances as on March 31, 2022 (92.57% as on March 31, 2021). Slippages have remained low, given the significant share of the refinance segment, which consists of banks and high rated NBFCs. However, SIDBI has witnessed slippages from its NBFC exposures in the past, including slippages of ~Rs. 1,031 crore (largely comprising a single NBFC exposure) in FY2022. As a result, the fresh NPA generation stood at 0.66% in FY2022, which was higher than 0.08% in FY2021. However, SIDBI made full provisions on the said exposure and wrote off the same in FY2022. As a result, the gross NPA (GNPA) and NNPA ratios remained strong at 0.11% and 0.06%, respectively, as on June 30, 2022 (0.11% and 0.07% as on March 31, 2022 and 0.18% and 0.12%, respectively, as on March 31, 2021).

The asset quality indicators in the direct lending book had been comparatively weaker than the refinance book in the past, although the impact on the overall asset quality metrics has been limited as the overall share in advances is low. Further, the restructured book stood at 0.04% of the standard advances (5.87% of the direct lending book) and could be a source of near-term stress, although it remains manageable and limited in relation to the bank's operating profit and net worth.

Funding profile remains strong with MSE fund allocations – SIDBI's funding profile remains dominated by low-cost MSE fund/Rural Infrastructure Development Fund (RIDF) allocations. It has access to these low-cost funds, which are made available by banks against their shortfalls in meeting their priority sector lending (PSL) targets. The total borrowings under the MSE fund programme remained dominant at Rs. 1.41 lakh crore and comprised 67% of its overall borrowings as on March 31, 2022. Given its quasi-sovereign status, SIDBI mobilises funds at competitive rates from the capital markets in the form of bonds, commercial papers and certificates of deposit.

MSE/RIDF allocation for FY2023 was higher at Rs. 65,000 crore (compared to Rs. 55,000 crore in FY2022 and Rs. 40,000 crore in FY2021). In addition to this, in FY23, SIDBI has undrawn allocation of Rs. 5,000 crore towards refinance in credit-deficient districts and Rs. 5,000 crore towards regular refinance and un-drawn allocation of Rs 6,206 crore under the Cluster Development Fund. Continued allocations under MSE funds will remain important for SIDBI for maintaining a competitive cost of funds as well as the scale of its refinancing business and hence its profitability. Given the growth targets for FY2023, the RIDF allocations are expected to remain the dominant source of funding for SIDBI.

Credit challenges

Growth linked to availability of low-cost MSE fund allocations/RIDF deposits and refinance demand – SIDBI's growth prospects remain linked to the extent of coverage achieved by SCBs in meeting their PSL targets. As SCBs progressively achieve higher PSL targets, the overall allocation under MSE funds could drop, thereby affecting the growth prospects in the long term. Moreover, the MSE fund allocation of Rs. 2.48 lakh crore for FY2018-23 has, to a major extent, supported SIDBI's overall growth. Additionally, PSL shortfalls are allocated to other eligible AIFIs like National Housing Bank (NHB) and National Bank for Agriculture and Rural Development (NABARD) apart from Micro Units Development & Refinance Agency Ltd. (MUDRA). The annual allocation to SIDBI will also remain dependent on its relative importance compared to other AIFIs, which could result in lower allocations in case of increased allocation or preference to others.

Net advances grew by ~29% on a YoY basis to Rs. 2.02 lakh crore as on March 31, 2022 from Rs. 1.56 lakh crore as on March 31, 2021 driven by an increase in demand for refinance in H2 FY2022. In contrast, net advances de-grew by 6% in FY2021 largely on account of the surplus liquidity environment in the banking system. Going forward, the overall growth momentum is likely to continue, given the narrowing systemic liquidity levels. This could result in a sharper rise in the cost of wholesale deposits in relation to refinancing from FIs like SIDBI, which is likely to remain more competitively priced apart from being free of statutory liquidity ratio (SLR)/cash reserve ratio (CRR) requirements.

Relatively concentrated exposure in indirect lending segment – SIDBI's lending is concentrated towards SCBs (82% as on March 31, 2022) followed by private sector entities excluding banks (7%) and NBFCs (~9%). With a high share of refinancing to banks, the concentration of the top 20 borrowers in the total exposure remained high at ~68% as on March 31, 2022 (~69% as on March 31, 2021). This is, however, mitigated by the limited credit risk in the refinance portfolio of banks.

Modest earnings profile, mainly driven by fixed margins in refinance book – Given the cap on lending margins in the refinance business and the high share of MSE refinance, the earnings profile, in terms of the RoA, remains modest. Further, the gross interest spreads narrowed to 1.02% in FY2022 (1.47% in FY2021), as the yields on advances witnessed a relatively sharper moderation in relation to the decline in the cost of funds. Similarly, the net interest margins (NIM/Average total assets) moderated to 1.37% in FY2022 from 1.94% in FY2021, leading to a drop in the operating profitability level to 1.21% in FY2022 (2.07% in FY2021). However, despite the relative spike in credit costs on the back of a lumpy NBFC slipping during the year, credit costs remained in check at 0.16% in FY2022 (0.23% in FY2021) partly supported by utilization of floating provisions. Nevertheless, the earnings profile moderated with an RoA and RoE of 0.89% and 7.96%, respectively, in FY2022 (1.26% and 11.27%, respectively, in FY2021). Going forward, any regulatory change, resulting in the narrowing of spreads, will remain a key monitorable for SIDBI's profitability.

Liquidity position: Superior

As a large part of SIDBI's loan book comprises refinance with a three-year tenure, which is largely funded through RIDF deposits with a similar maturity, the overall asset and liability management (ALM) profile remains well matched to a large extent. As a result, SIDBI had positive cumulative asset-liability gaps across all maturity buckets as on June 30, 2022. Further, SIDBI has undrawn lines of ~Rs. 12,500 crore from banks and RIDF allocations of ~Rs. 65,000 crore as on date, which can be called on short notice and can be drawn to meet any shortfall/funding gaps in future.

Rating sensitivities

Positive factors – Not applicable

Negative factors – ICRA could assign a Negative outlook or downgrade the rating in case of a dilution in SIDBI's strategic role and importance to the GoI.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA Rating Methodology for Banks Impact of Parent or Group Support on Issuer's Credit Rating ICRA's Policy on Withdrawal of Credit Ratings
Parent/Group support	ICRA expects SIDBI to remain important to the GoI for supporting the growth of the MSME sector in India and expects the GoI to provide financial support, including MSE fund allocation and capital, if required
Consolidation/Standalone	For arriving at the rating, ICRA has considered the standalone financials of SIDBI. However, in line with its limited consolidation approach, ICRA has factored in the capital requirement of SIDBI's subsidiaries. In ICRA's view, the subsidiaries will remain self-sufficient in meeting their capital requirements in the near to medium term

About the company

Small Industries Development Bank of India (SIDBI) is an FI, constituted under an Act of Parliament (SIDBI Act, 1989), for the promotion and development of the MSME sector in India. SIDBI is jointly owned by the GoI (largest shareholder with a stake of 20.85% as on March 31, 2022), SBI (15.65%), LIC (13.33%) and other PSBs (the balance). ICRA notes that the GoI directly controls the operations of all the shareholders of SIDBI, which indirectly gives it total access to SIDBI's operations.

SIDBI's board of directors consists of –

- The Chairman & Managing Director appointed by the Central Government (for a term of 3 years)
- Two whole-time directors appointed by the Central Government
- Two directors who shall be officials of the Central Government
- Three directors to be nominated in the prescribed manner by the development bank, the PSBs, General Insurance Corporation of India (GIC), LIC and other institutions owned or controlled by the Central Government
- Three directors, including one from the officials of the state financial corporations, nominated by the Central Government from among persons with special knowledge of or professional experience in science, technology, economics, industry, banking, industrial cooperatives, law, industrial finance, investment, accountancy, marketing or any other matter
- Such number of directors, not exceeding four, elected in the prescribed manner by shareholders other than the development bank, the PSBs, GIC, LIC and other institutions owned or controlled by the Central Government

Key financial indicators (standalone)

	FY2020	FY2021	FY2022	Q1 FY2023
Net interest income	3,299	3,679	3,012	1,134
Profit after tax	2,315	2,398	1,958	776
Net advances (Rs. lakh crore)	1.65	1.56	2.02	NA
Total assets (Rs. lakh crore)	1.88	1.92	2.47	NA
NIM/ATA	1.92%	1.94%	1.37%	NA
RoA	1.35%	1.26%	0.89%	1.20%*
RoE	12.18%	11.27%	7.96%	NA
Tier I	26.62%	27.49%	24.26%	NA
CRAR	26.62%	27.49%	24.28%	21.53%
Gross NPA	0.63%	0.18%	0.11%	0.11%
Net NPA	0.40%	0.12%	0.07%	0.06%
PCR (excl write-offs)	36.6%	34.5%	39.5%	41.4%

*Source: SIDBI & ICRA Research; Amount in Rs. crore unless mentioned otherwise ; * As per SIDBI-Financial results for the quarter ended June 30, 2022.*
All ratios as per ICRA's calculations

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Sr. No.	Name of Instrument	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years				
		Type	Rated Amount (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2023	FY2022			FY2021	FY2020
					Aug-17-2022	Mar-17-2022	Feb-22-2022	Jan-10-2022	Jan-13-2021	Dec-31-2019
1	Long-term bonds programme	Long term	20,000.00*	-	[ICRA]AAA (Stable)					
2	Long-term bonds programme	Long term	18,635.00*	16,425.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
3	Long-term bonds programme	Long term	1,365.00	-	[ICRA]AAA (Stable); withdrawn	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)

Source: ICRA Research
**Balance yet to be placed/to be placed – Bonds of Rs. 22,210.00 crore as on August 11, 2022*

Complexity level of the rated instrument

Instrument	Complexity Indicator
Long-term bonds	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instruments credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: www.icra.in

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE556F08JK7	Long-term bonds	Apr-26-2019	7.95%	Apr-26-2022	1,365.00	[ICRA]AAA (Stable) withdrawn
INE556F08JP6	Long-term bonds	Feb-27-2020	6.27%	Feb-27-2023	620.00	[ICRA]AAA (Stable)
INE556F08JQ4	Long-term bonds	Aug-18-2020	4.90%	Aug-18-2023	500.00	[ICRA]AAA (Stable)
INE556F08JR2	Long-term bonds	Dec-17-2020	4.58%	Dec-18-2023	250.00	[ICRA]AAA (Stable)
INE556F08JV4	Long-term bonds	Mar-02-2022	5.57%	Mar-03-2025	2,500.00	[ICRA]AAA (Stable)
INE556F08JW2	Long-term bonds	Mar-16-2022	5.40%	Mar-17-2025	1,525.00	[ICRA]AAA (Stable)
INE556F08JX0	Long-term bonds	Mar-28-2022	5.70%	Mar-28-2025	1,625.00	[ICRA]AAA (Stable)
INE556F08JY8	Long-term bonds	May-31-2022	7.15%	Jun-2-2025	2,500.00	[ICRA]AAA (Stable)
INE556F08JZ5	Long-term bonds	Jul-18-2022	7.15%	Jul-21-2025	3,000.00	[ICRA]AAA (Stable)
INE556F08KA6	Long-term bonds	Jul-28-2022	7.25%	Jul-31-2025	3,905.00	[ICRA]AAA (Stable)
Unplaced	Long-term bonds	Unutilised	NA	NA	22,210.00	[ICRA]AAA (Stable)

Annexure II: List of entities considered for consolidated analysis

S. No.	Name of the Entity	Ownership	Consolidation Approach
1.	**MUDRA Ltd.**	100.0%	Limited Consolidation
2.	**SIDBI Venture Capital Ltd (SVCL)**	100.0%	Limited Consolidation
3.	**SIDBI Trustee Company Ltd**	100.0%	Limited Consolidation

Source: SIDBI and ICRA Research

ANALYST CONTACTS

Karthik Srinivasan
+91 22 6114 3444
karthiks@icraindia.com

Anil Gupta
+91 124 4545 314
anilg@icraindia.com

Gayatri Kulkarni
+91 22 6114 3471
gayatri.kulkarni@icraindia.com

Aashay Choksey
+91 22 6114 3430
aashay.choksey@icraindia.com

Aayush Behal
+91 124 4545 386
aayush.behal@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches