Moody's places Yes Bank's ratings under review for downgrade

RATING RATIONALE

The review for downgrade takes into account Moody's expectation that the ongoing liquidity pressures on Indian finance companies will negatively impact the credit profile of Yes Bank, given the bank's sizeable exposure to weaker companies in the sector. At the end of March 2019, Yes Bank's exposure to Indian housing finance companies (HFC) and non-bank finance companies (NBFC) represented 6.4% of its total exposure. In addition, Yes Bank had a 7% direct exposure to the commercial and residential real estate sector as of the same date, which is also under pressure, because liquidity conditions have worsened for the real estate sector, just like with the HFCs and NBFCs.

In April 2019, the bank classified about INR100 billion of its exposures, representing 4.1% of its total loans under the watchlist, that could translate into nonperforming loans over the next 12 months.

Taking into account the bank's own disclosure of the stressed book, as well as Moody's expectation of stress in the Indian HFC, NBFC and real estate sectors, Moody's expects significant pressure on the bank's asset quality and therefore profitability and capital position. Nevertheless, the impact will be somewhat cushioned by the bank's proactive loan loss provisioning for anticipated stress. During the fiscal year ended March 2019 (fiscal 2019), the bank made loan loss provisions of about 20% for the loans on the watchlist.

The bank's weak performance in fiscal 2019 led to its capital, as measured by the common equity tier 1 ratio, falling to 8.4% from 9.7% in fiscal 2018.

The bank's board has approved an up to USD1 billion equity capital raise. If Yes Bank cannot raise the capital, its loss absorbing capacity and therefore financial profile will be under pressure.

In this rating action, Moody's has maintained the negative adjustment for corporate behavior for Yes Bank, which results in a one notch adjustment to the bank's standalone credit profile (the BCA) when compared to the bank's financial profile. The negative adjustment takes into account management's aggressive strategy, which has translated into rapid loan growth in the past 4-5 years and large concentrations to some of the Indian conglomerate groups. The adjustment also takes into account the Reserve Bank of India's (RBI) identification of several lapses and regulatory breaches in the various areas of the bank's functioning.

In Moody's opinion, given the recent changes at the bank, its corporate behavior can gradually improve. Nevertheless, Moody's continues to make the negative adjustment to reflect the fact that the changes are fairly new and our expectation that the impact of the previous actions will continue to negatively impact the financial performance of the bank.

The recent changes at the bank — as referenced above — include the appointment of an external candidate as MD and CEO, Mr. Ravneet Gill, and the appointment by the RBI of a retired RBI Deputy Governor, Mr. R. Gandhi, as an additional director at the Board of the bank.

Moody's continues to maintain its assumption of a moderate probability of government support for deposits and senior unsecured debt, reflecting the bank's modest, but rapidly growing franchise, and relative importance to India's banking system. This support assumption results in a one notch uplift to the bank's foreign currency issuer rating of Ba1 from its BCA of ba2.

In the review for downgrade, Moody's will consider the developments in the bank's solvency profile, namely, asset quality, capital, profitability, as well as any impact from the solvency pressures on its funding and liquidity profile. Moody's will also review the bank's corporate behavior in light of the changes made and being made in the operations and strategy of the bank.

WHAT COULD CHANGE THE RATING UP

Given the review for downgrade, Moody's will unlikely upgrade the bank's ratings over the next 12-18 months.

Nevertheless, Moody's could change the ratings outlook to stable if Yes Bank (1) maintains its current asset quality profile, and/or adequately provides for the stock of stressed assets; (2) strengthens its loss absorbing buffers by raising equity capital to bring its capital ratios in line with those of its similarly rated peers in India; and (3) meaningfully reduces concentration risk on the asset side and improves its liability profile.

WHAT COULD CHANGE THE RATING DOWN

Moody's could downgrade Yes Bank's ratings if (1) there is a sustained deterioration in impaired loans or loan-loss reserves, or if the rate of new nonperforming loan formation is significantly higher than previously experienced; or (2) the bank's capital ratios decline because of its inability to raise new capital, or both.

The principal methodology used in these ratings was Banks published in August 2018. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Yes Bank Limited is headquartered in Mumbai and reported total assets of INR3.8 trillion ($54.7 billion) at 31 March 2019.

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