केनरा बैंक Canara Bank

सिंडिकेट Syndicate

Ref:: SD:1598/1599/11/12::2020 **04.12.2020**

The Vice President **BSE Ltd.** **Phiroze Jeejeebhoy Towers** **Dalal Street** **MUMBAI - 400 001**	**The Vice President** **Listing Department** **National Stock Exchange of India Ltd** **EXCHANGE PLAZA** **Bandra-Kurla Complex, Bandra [E]** **MUMBAI - 400 051**

Dear Sir/Madam,

Sub : Affirmation / Revision of Ratings by Fitch Ratings
Ref : Disclosure under Regulation 30 of SEBI (LODR) Regulations, 2015

The Exchanges are hereby informed that the Fitch Ratings ("The Rating Agency") has affirmed / revised the ratings of Canara Bank and published the ratings on their website on December 3, 2020, as under :

Sl No.	Particulars	Existing Rating	Revised Rating
1.	Long-Term Issuer Default Rating (IDR)	'BBB-'	Affirmed at 'BBB-'; Outlook Negative
2.	Viability Rating (VR)	'bb-'	'b+'

The details of the ratings along with the rating rationale are available on their website (www.fitchratings.com). A copy of the rating is also enclosed herewith.

This is for your information and appropriate dissemination.

Yours faithfully,

कृते केनरा बैंक
For CANARA BANK

सहायक महा प्रबधक और कंपनि सचिव
Assistant General Manager & Company Secretary
VINAY MOHTA
COMPANY SECRETARY

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FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Canara Bank's IDR at 'BBB-', Outlook Negative; Downgrades VR

Thu 03 Dec, 2020 - 7:46 AM ET

Fitch Ratings - Singapore - 03 Dec 2020: Fitch has affirmed India-based Canara Bank's Long-Term Issuer Default Rating (IDR) at 'BBB-'. The Outlook is Negative. At the same time, Fitch has downgraded the bank's Viability Rating (VR) to 'b+' from 'bb-'.

The VR downgrade reflects a sharp and unexpected deterioration in Canara's core capitalisation as a result of its merger with Syndicate Bank, a mid-sized state bank. The dip in Canara's common equity Tier 1 (CET1) ratio to 8.2% has heightened capital risk amid a challenging operating environment, which threatens the bank's asset quality and earnings. Canara's weakened loss-absorption capacity renders its intrinsic creditworthiness vulnerable to further downside if capitalisation is not adequately replenished. We expect the government to inject capital, if required, but the bank may need to supplement this to maintain adequate capital levels.

The Negative Outlook on the IDR mirrors the Outlook on India's sovereign rating of 'BBB-' due to the impact of the escalating coronavirus pandemic on India's economy. See "Fitch Revises India's Outlook to Negative, Affirms IDR at 'BBB-'", at www.fitchratings.com/site/pr/10126674.

The operating environment for Indian banks remains challenging, despite a moderate revival in economic activity due to the gradual easing of the lockdown since May 2020. We revised our forecast for India's real GDP growth for the financial year ending March 2021 (FY21) to -10.5%, from -5.0% in September 2020. We believe growth will rebound to 11.0% in FY22, which will mainly reflect the effects of a low base. The economic contraction is likely to result in protracted weakness in the asset-quality cycle, which could be manifested in an increase in stressed loans and, ultimately, more write-offs over the next few years, even though Indian banks' latest 2QFY21 earnings present a more benign picture. (See "Indian Banks to Face Tough Times" at www.fitchratings.com/site/re/10137748).

A speedy economic recovery would allow the sector to rebound meaningfully, absent which we expect weak prospects for new business and revenue for the Indian banking sector in 2021.

KEY RATING DRIVERS

IDRS, SUPPORT RATING AND SUPPORT RATING FLOOR

Canara's Long-Term IDR is driven by its Support Rating and Support Rating Floor, which reflects our expectation of extraordinary government support, if required, based on the bank's high systemic importance and state linkages. This is driven by Canara's reasonable post-merger market share of 6% of sector assets and 7% of deposits, a pan-India franchise and 78.6% state ownership.

State-owned banks, such as Canara, often play an important policy role in furthering the state's social-lending objectives and are thus important for financial inclusion. Fitch believes that a default by a large bank, like Canara, would result in a general loss of confidence in the sector and pose high reputational risk for the state.

SENIOR DEBT

Canara's senior debt rating is at the same level as its IDR, as the debt represents its unsecured and unsubordinated obligations.

VIABILITY RATING

Canara's VR is two notches below our 'bb' assessment of India's operating environment and four notches below its IDR to reflect a weak intrinsic risk profile. We do not believe that Canara's core capitalisation is commensurate with risks and think the bank is vulnerable to even moderate shock. The acquisition of a weaker state bank in April 2020 has elevated these vulnerabilities, which include a small capital buffer, high impaired loans and less-than-satisfactory pre-provision profit amid a challenging operating environment. The heightened capital risk and above-average impaired loans are of high influence on the bank's VR and more consistent with a lower VR rating, despite our expectations of ordinary state support. The bank's pan-India franchise ensures continued stable funding and liquidity, which, though positive, is offset by weaknesses in other areas and is therefore less influential on the VR.

The bank's CET1 ratio of 8.2% in 1HFY21 is close to the regulatory minimum requirement of 8.0%, which has been deferred to April 2021 due to the pandemic. The vulnerability of capital to even moderate shock is visible in the bank's high net impaired loans/CET1 ratio of 49%, despite improved loan loss cover of 61% (FY20: 51%). However, provision levels are weaker compared with that of peers.

We have a negative outlook on capitalisation as we do not think Canara's planned equity raising of INR20 billion (40 bp of 1HFY21 risk-weighted assets) will significantly improve capital buffers. While there is a possibility that Canara might raise an additional INR30 billion in fresh equity by FY21, Fitch estimates that the CET1 ratio would be no better than that of lower-rated peers even if the entire amount of INR50 billion were to be raised by the bank, unless the state injects significant capital into the bank. Then again, Canara's peers are also looking to bolster their capital buffers. However, raising capital remains a challenge for state banks, including Canara due to its diminished price/book value of 0.3x.

Canara's impaired-loan ratio was stable, at 8.2% in 1HFY21, due to lower slippages with support from regulatory measures, such as loan moratoriums, and continued write-offs. However, we do not expect this trend to continue, as the ratio does not reflect the economic realities of the prevailing slowdown. The bank had a high 23% share of loans under moratorium in 1HFY21 and its "special mention" loans - those overdue by 0-90 days - stood at 4.3% of total loans. We believe there is a high risk for asset-quality deterioration over the medium term, starting 3QFY21, especially if the pace of economic recovery is constrained. However, not all stressed assets will be recognised as impaired loans, since a one-time loan-restructuring scheme for COVID-19 affected loans and the ability to refinance with banks could structurally delay recognition of potential stress over the next two years. Nevertheless, we would treat restructured loans as stressed loans as part of our analysis, as we have done in the past.

We see heightened risks from SME loans, which comprised 17% of Canara's loans in 1HFY21, although government-sponsored schemes may alleviate stress to some degree. Retail loans, at 17% of loans, are likely to be more resilient, although stronger-than-average growth in FY19 and FY20 indicates somewhat lower seasoning, particularly for unsecured retail loans. We expect stress in corporate sectors, such as tourism, non-bank financial institutions, infrastructure, auto, construction and real estate; these sectors cumulatively constituted nearly 34% of total loans in 1QFY21. The stress is more likely to be present in locally rated sub-investment-grade loans, which represented 6.9% of loans in 1HFY21 (FY20: 6.5%) and had an increase in delinquency rate to 4.3% in 1HFY21 (FY20: 3.1%). Pandemic-related contingency provisions add 1.9% to loan loss cover, which is insufficient to provide adequate protection in case of substantial slippages.

Canara's operating profit/risk-weighted assets improved to 0.42% in 1HFY21, but offers little protection against stress, as loan impairment charges constituted nearly 88% of pre-provision profit. We do not think an earnings recovery will be sustainable should slippages and loan impairment charges rise, as reflected in our negative outlook on earnings and profitability. We expect Canara's profitability to exhibit a certain degree of structural weakness until balance sheet stress is adequately dealt with.

Canara's deposit share remains steady, despite the economic stress. This reflects continued depositor confidence due to the bank's state ownership. Liquidity is also adequate, with excess liquidity holdings of 6% and a liquidity coverage ratio of 125%.

RATING SENSITIVITIES

IDRS, SUPPORT RATING, SUPPORT RATING FLOOR AND SENIOR DEBT

Factors that could, individually or collectively, lead to negative rating action/downgrade:

The Support Rating and Support Rating Floor are sensitive to our assessment of the government's propensity and ability to support the bank, based on its size, systemic importance and state linkage. Weakening of the government's ability to provide extraordinary support - reflected by negative action on India's sovereign ratings - would lead to negative action on the IDR. A downgrade is also probable should Fitch perceive any reduction in the government's propensity to extend timely support, in which case we will reassess the Support Rating and Support Rating Floor and, in turn, the bank's IDR and senior debt ratings, although this is not our base case.

The senior debt ratings will be downgraded if the bank's Long-Term IDR is downgraded.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

Canara's IDR is driven by its Support Rating Floor; a revision of our Outlook on the sovereign rating to Stable would lead us to revise the Outlook on Canara to Stable, provided the sovereign's propensity to provide support remains unchanged. The IDR could be upgraded upon a sovereign upgrade if we believe the sovereign's ability and propensity to support the bank has improved. However, an upgrade of the sovereign rating appears less probable in the near term. An upgrade of the VR is unlikely to affect the bank's IDR, since the IDR is four notches above the VR.

The senior debt ratings will be upgraded if the bank's Long-Term IDR is upgraded.

VR

Factors that could, individually or collectively, lead to negative rating action/downgrade:

We are likely to downgrade the VR if the bank's CET1 ratio falls below the minimum 8% threshold that banks are required to maintain from April 2021; this would be consistent with a lower 'b' VR if not sufficiently replenished. Capital impairment could stem from a deterioration in the stressed-loan ratio - impaired loans + restructured loans approaching 15% (from impaired loan ratio of 8.2% at end-1HFY21) - which would be likely to cause losses and impact already-weak capitalisation.

A downgrade of the VR to the 'ccc' category would be in order if poor earnings and weak asset quality, with a stressed-asset ratio at or above 20%, compromised the bank's core capital position and increased the need for extraordinary support on a last-resort basis. However, this is not our base case, as we believe there is a high likelihood of fresh capital from the state well ahead of any breach of regulatory requirements. We believe Canara's assistance for clients through the downturn will become less effective over time, which will limit the speed of recovery after the pandemic is brought under control.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

A VR upgrade is not probable in the near term in light of the risks to the bank's intrinsic profile, considering rising external pressure from the pandemic and merger. Pressure on the VR would ease if an economic recovery was quicker and stronger than we envisage, as this could stabilise asset quality and capitalisation. We expect the CET1 ratio to approach 12% and the impaired-loan ratio to fall towards 5% (from impaired loan ratio of 8.2% at end-1HFY21) before considering a VR upgrade.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [https://www.fitchratings.com/site/re/10111579]

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Canara has an ESG Relevance Score of '4' for Governance Structure. It reflects our assessment that key governance aspects, in particular board independence and effectiveness, ownership concentration and protection of creditor or stakeholder rights are a moderate influence on VR. It is a negative influence since Fitch views governance to be less developed, which is evident from weak underwriting that results in high levels of poorly performing loans and credit losses. The board is dominated by government appointees, and business models often focus on supporting government strategy with lending directed towards promoting socioeconomic and macroeconomic policies, which may include lending to government-owned companies. These factors also drive our view on the bank's state linkages that affect support prospects that drive the long-term ratings.

Canara also has an ESG Relevance Score of '4' for Financial Transparency. It reflects our assessment that the quality and frequency of financial reporting and the auditing process have a moderate influence on the VR. It is a negative influence however since these factors have become more prominent in the past few years because of the sharp financial deterioration at state banks as well as the widely reported divergences in non-performing loan recognition between the banks and the regulator, although these incidences have narrowed in recent years. Still, financial transparency is viewed pivotal for general business and depositor confidence and can lead to significant reputational risk if not managed well.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
Canara Bank	LT IDR	BBB- Rating Outlook Negative	Affirmed	BBB- Rating Outlook Negative
	ST IDR	F3	Affirmed	F3
	Viability	b+	Downgrade	bb-
	Support	2	Affirmed	2
	Support Floor	BBB-	Affirmed	BBB-
• senior unsecured	LT	BBB-	Affirmed	BBB-

VIEW ADDITIONAL RATING DETAILS

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Additional information is available on www.fitchratings.com

APPLICABLE CRITERIA

Bank Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Canara Bank	EU Endorsed

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