



पंजाब नैशनल बैंक



punjab national bank

Share Department, Board & Coordination Division, Plot No.4 Sector 10, Dwarka, New Delhi-110075
Tel No: 011-28044857 E-mail: hosd@pnb.co.in

Scrip Code : PNB	Scrip Code : 532461
The Asstt. Vice President National Stock Exchange of India Limited "Exchange Plaza" Bandra – Kurla Complex, Bandra (E) Mumbai – 400 051	The Dy General Manager BSE Limited 1 st Floor, Phiroze Jeejeebhoy Towers, Dalal Street, Mumbai – 400 001

Date: 23.11.2021

Dear Sir (s),

Reg.: Rating Action by Fitch Ratings.

The Exchange is hereby informed that Fitch Ratings vide its rating action dated 22.11.2021 has **affirmed** PNB's Long-Term Issuer Default Rating (IDR) at 'BBB-', with a Negative Outlook. The Agency has also **affirmed** the Bank's Viability Rating (VR) at 'b' and has **assigned** the Bank a Government Support Rating (GSR) of 'bbb-', which drives the IDR.

Fitch Ratings has **withdrawn** Support Rating and Support Rating as per its updated Bank Rating Criteria.

This is in compliance with Regulation 30 of SEBI (LODR) Regulations, 2015.

Thanking you

Yours faithfully,

(Ekta Pasricha)
Company Secretary



Encl.: as above



RATING ACTION COMMENTARY

Fitch Affirms Punjab National Bank at 'BBB-'; Outlook Negative

Mon 22 Nov, 2021 - 3:25 AM ET

Fitch Ratings - Singapore/Mumbai - 22 Nov 2021: Fitch Ratings has affirmed Punjab National Bank's (PNB) Long-Term Issuer Default Rating (IDR) at 'BBB-'. The Outlook is Negative. This reflects the Outlook on India's sovereign rating (BBB-/Negative). The agency has also affirmed PNB's Viability Rating (VR) at 'b'. In line with the updated Bank Rating Criteria, we have assigned PNB a Government Support Rating (GSR) of 'bbb-', which drives the IDR. A full list of rating actions is below.

The operating environment (OE) outlook of Indian banks has been revised to stable from negative, reflecting a better recovery than we expected in business and economic activity following the Covid-19 pandemic second wave. The 'bb' OE score is higher than the implied score of 'b', reflecting our view that India's economy will generate sustainable business growth opportunities.

Economic momentum and regulatory measures should support modest improvements in Indian banks' financial profiles over the next 12-24 months, even though challenges remain.

Fitch is withdrawing PNB's Support Rating and Support Rating Floor as they are no longer relevant to the agency's coverage following the publication of our updated Bank Rating Criteria on 12 November 2021.

KEY RATING DRIVERS

IDRS AND GOVERNMENT SUPPORT RATING

PNB's Long-Term IDR is driven by its GSR of 'bbb-', which is same as India's sovereign rating. It reflects Fitch's expectation of a high probability of extraordinary government support for PNB, if required, because of the bank's high systemic importance. It stems from PNB's position as the second-largest state-owned bank, its pan-India franchise and majority state ownership at 73.2% as of September 2021.

Large state-owned banks such as PNB also play an important role in furthering the state's objectives of social-lending and financial inclusion, which further underscores their importance. Fitch believes a failure or default by a large state-owned bank such as PNB could lead to loss of confidence in the banking sector and significant reputational risk for the state.

The Negative Outlook on the Long-Term IDR mirrors the Outlook on India's sovereign rating; see [Fitch Affirms India at 'BBB-'; Outlook Negative](#).

VIABILITY RATING

PNB's VR of 'b' is one notch below its implied VR, reflecting our view that the bank's risk profile has a greater impact on the VR than is implied by its weighting. It is reflected in PNB's risk control weaknesses that have resulted in higher impaired loans and losses (relative to most peers), while control lapses have weighed on its financial metrics in the past several years.

Our assessment factors in some potential deterioration in financial metrics (not our base case over the next two years) as forbearance unwinds - particularly asset quality, but we view the VR to be relatively stable at the current rating level, unless Covid-related loan losses exceed our expectations.

The VR also factors PNB's business profile, including its large franchise and business model. However, this does not drive the VR, which also considers the scope for a meaningful improvement in management and governance standards, similarly to other Indian state banks. Therefore, PNB's business profile score of 'bb+' is below the implied category score of 'bbb' because management and governance have a greater bearing on the bank's risk profile and financial performance, and also influences its ability to defend market position more than its size and business profile may suggest.

Fitch has maintained PNB's capitalisation and leverage score at 'b+', which is aligned with the implied score. We have revised the outlook to stable from negative to reflect our view that the recent improvement in PNB's capital buffers should remain stable over the next two years.

PNB's common equity Tier 1 (CET1) ratio increased to 11.6% in the first-half of the financial year ending March 2022 (1HFY22) (FY20: 10.0% adjusted for merger), driven by a fresh equity injection of USD0.8 billion since December 2020 and moderating risk density.

We note that PNB has not earmarked any further fresh equity raising, which leaves its buffers potentially vulnerable because of its high net impaired loans/CET1 ratio of 54% in 1HFY22. Capital augmentation would further insulate the balance sheet against unexpected stress, which may emerge after FY23 as regulatory forbearance begins wearing off. However, Fitch expects further capital support (if needed) from the state shareholder, which should mitigate risks.

PNB's asset quality score has been maintained at 'b-', in line with the implied category score. Fitch has revised the outlook to stable from negative, as we expect the four-year average impaired loans ratio to decline slightly over the next two years because of regulatory relief on fresh stress and gradual winding down of legacy bad loans.

PNB's impaired loans ratio improved to 13.6% in 1HFY22 (FY20: 14.2%), but there are still some vulnerabilities because the guaranteed portion of emergency loans accounted for 1.7% of loans while Covid-restructured loans were at 2.4% of loans. We expect some pressures to emerge post-FY23, as and when forbearance begins wearing off.

PNB's earnings and profitability score has been revised up to 'b-' from 'ccc-', in line with the implied score, and the outlook is stable. It reflects Fitch's view that structural challenges to PNB's earnings have receded and that we expect the bank to report modest profitability over the near to medium term.

PNB's operating profit/risk-weighted assets (RWA) ratio improved to 0.7% in 1HFY22 (FY21: 0.6%), driven by lower credit costs (1HFY21: 1.6%, FY21: 2.4%, FY20: 3.1%), although pre-emptive Covid-19 provisions are limited. Impairment charges were relatively high at 79% of pre-provision operating profit at 1HFY22.

PNB's funding and liquidity profile is stable, and is scored 'bbb-', which is above the implied category score of 'bb'. We have applied "deposit structure" as a positive adjustment, as PNB will continue to benefit from high depositor confidence due its strong linkages with the state.

PNB's low-cost deposit share has improved amid the uncertain environment (1HFY22: 45% of deposits, FY20: 42% adjusted for merger) and stable liquidity is reflected in its high liquidity coverage ratio of 191% (FY21). The loan/deposit ratio has been declining (1HFY22: 66%, FY20: 69%), and Fitch expects the trend to reverse as loan growth revives.

RATING SENSITIVITIES

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

IDRS AND GOVERNMENT SUPPORT RATING

The GSR is most sensitive to Fitch's assessment of the government's propensity and ability to support PNB, based on the systemic importance, which is driven by its market position and the state's controlling ownership of 73.2%. Weakening of the government's ability to provide extraordinary support - reflected by negative action on the sovereign rating - would lead to a similar action on the Long-Term IDR.

A downgrade to the Long-Term IDR is also likely if we believe that the government's propensity to extend timely support to PNB has decreased, in which case the agency will reassess the GSR and Long-Term IDR, although that is not our base case.

VIABILITY RATING

PNB's VR could be vulnerable to deterioration in the business and economic environment, although we view it to be stable for the next one to two years. A downgrade is less likely in our base scenario, but it is possible if the bank's risk profile becomes a more binding constraint on the bank's modest loss-absorption buffers or if it were to have higher deterioration than we expect in key financial parameters. The latter could manifest through a combination of one or more of the three factors below and a weaker risk profile, assuming our assessment of business profile remains unchanged:

- the four-year average impaired loans ratio approaching 20%;
- resurgence of losses which puts PNB's structural profitability in doubt; and
- significant drop in PNB's CET1 ratio from current levels, and closer to the regulatory minimum of 8%, without a credible plan to restore it to closer to 12% or above.

However, a lower business profile score - though not our base case - can also lead to a VR downgrade if it is also accompanied by the above three conditions being met, without any changes to risk profile.

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

IDRS AND GOVERNMENT SUPPORT RATING

PNB's Long-Term IDR is driven by its GSR. A revision of the sovereign rating Outlook to Stable would lead to a corresponding change in the Outlook for PNB's Long-Term IDR, provided the sovereign's propensity to support remains unchanged. An upgrade to PNB's GSR and Long-Term IDR could occur in the event of a sovereign upgrade if Fitch believes that the sovereign's ability and propensity to support the bank has improved. However, an upgrade of the sovereign rating appears less certain in the near term, considering the Negative Outlook.

VIABILITY RATING

A VR upgrade is possible if the score is revised upwards for at least two or more of the KRDs. It could manifest in stronger key financial metrics, such as a combination two or more of the factors mentioned below assuming our assessment of business profile remains unchanged:

- the CET1 ratio is sustained closer to 12%;
- the four-year average impaired loans ratio dropping below 10%;
- the four-year average operating profit/RWA ratio approaching 1.25%.

PNB's risk profile will also remain an important consideration in determining whether the improvements to its financial metrics can be sustained.

VR ADJUSTMENTS

Fitch has used the risk profile as a negative adjustment factor to arrive at the assigned VR, as we believe the bank's risk profile has a greater impact than the weighting suggests. The risk profile has driven the bank's weak financial metrics, evident from its impaired loans being above the average, volatile earnings and thin core capital buffers.

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.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

The Outlook and PNB's Long-Term IDR are the same as India's sovereign rating and is thus directly linked with the sovereign IDR via the GSR, which reflects our view of the probability of extraordinary state support, should there be a need.

ESG CONSIDERATIONS

Punjab National Bank 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, yet negative for PNB's credit profile, and relevant to the ratings in conjunction with other factors. These factors have become more prominent in the past few years, given the sharp financial deterioration at state banks and widely reported divergences in non-performing loan recognition between the banks and the regulator, although these incidences have narrowed in recent years.

Nonetheless, government and regulatory pandemic-related relief measures pose a risk for the transparent recognition of impaired loans. Still, financial transparency is viewed as pivotal for general business and depositor confidence and can lead to significant reputational risk if not managed well.

PNB has an ESG Relevance Score of '4' for Governance Structure, in line with other state banks. It reflects our assessment that key governance aspects, in particular board independence and effectiveness, ownership concentration and protection of creditor or stakeholder rights are of moderate influence, yet negative for PNB's credit profile, and relevant to the ratings in conjunction with other factors. Fitch views PNB's governance to be less developed, evidenced by significant lending to higher-risk borrowers and instances of weak oversight, which led to fraud charges in 2018. This has also led to high levels of stressed 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.

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 ⇅
Punjab National Bank	LT IDR	BBB- Rating Outlook Negative		BBB- Rating Outlook Negative
	Affirmed			
	ST IDR	F3	Affirmed	F3
	Viability	b	Affirmed	b
	Support	WD	Withdrawn	2
	Support Floor	WD	Withdrawn	BBB-
Government Support				bbb-
New Rating				

[VIEW ADDITIONAL RATING DETAILS](#)

FITCH RATINGS ANALYSTS

Tania Gold

Senior Director

Primary Rating Analyst

+65 6796 7224

tania.gold@fitchratings.com

Fitch Ratings Singapore Pte Ltd.

One Raffles Quay #22-11, South Tower Singapore 048583

Prakash Pandey

Associate Director

Secondary Rating Analyst

+91 22 4000 1773

prakash.pandey@fitchratings.com

Jonathan Cornish

Managing Director

Committee Chairperson

+852 2263 9901

jonathan.cornish@fitchratings.com

MEDIA CONTACTS

Bindu Menon

Mumbai

+91 22 4000 1727

bindu.menon@fitchratings.com

Leslie Tan

Singapore

+65 6796 7234

leslie.tan@thefitchgroup.com

Additional information is available on www.fitchratings.com

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APPLICABLE CRITERIA

[Bank Rating Criteria \(pub. 13 Nov 2021\) \(including rating assumption sensitivity\)](#)

ADDITIONAL DISCLOSURES

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Punjab National Bank

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