IPO Note

September 01, 2022

Tamilnad Mercantile Bank Limited

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20 YEARS

Issue Snapshot:

Issue Open: Sept 05 – Sept 07, 2022

Price Band: Rs. 500 – 525

*Issue Size: Rs 831.60 cr (Fresh issue of 15,840,000 eq sh)

Reservation for:

QIB	atleast	75% eq sh
Non Institutional	upto	15% eq sh
((including 1/3rd for applications between Rs.2 lakhs to Rs.10 lakhs))		
Retail	upto	10% eq sh

Face Value: Rs 10

Book value: Rs 374.41 (Mar 31, 2022)

Bid size: - 28 equity shares and in multiples thereof

100% Book built Issue

Capital Structure:

Pre Issue Equity:	Rs.	142.51 cr
*Post issue Equity:	Rs.	158.35 cr

Listing: BSE & NSE

Book Running Lead Managers: Axis Capital Limited, Motilal Oswal Investment Advisors Limited, SBI Capital Markets Limited

Registrar to issue: Link Intime India Private Ltd

Shareholding Pattern

Shareholding Pattern	**Pre issue %**	**Post issue %**
Promoter and Promoter Group	0.0	0.0
Public	100.0	100.0
Total	100.0	100.0

*=assuming issue subscribed at higher band
Source for this Note: RHP

Background & Operations:

Tamilnad Mercantile Bank Limited (TMBL) is one of the oldest and leading old private sector banks in India with a history of almost 100 years. It offers a wide range of banking and financial services primarily to micro, small and medium enterprises ("MSME"), agricultural and retail customers ("RAM"). As of March 31, 2022, it has 509 branches, of which 106 branches are in rural, 247 in semi-urban, 80 in urban and 76 in metropolitan centres. Its overall customer base is approximately 5.08 million as of March 31, 2022 and 4.05 million or 79.78% of its customers have been associated with it for a period of more than five years and have contributed to Rs. 350,142.39 million or 77.93% to its deposits and Rs. 219,022.26 million or 64.90% to its advances portfolios as of March 2022. It had the second highest Net Profit for Fiscal 2022 amongst its Peers, and its Return on Assets was also higher at 1.66% compared to a median 0.80% for its Peers for Fiscal 2022.

TMBL was incorporated as 'Nadar Bank Limited' in 1921 and its name was changed to 'Tamilnad Mercantile Bank Limited' in the year 1962. it received its license to carry on banking business from the Reserve Bank of India (the "RBI") in 1962. Since its incorporation, having head quartered at Thoothukudi, Tamil Nadu, India, it has built a strong presence in the state of Tamil Nadu, with 369 branches and 949 automated teller machines ("ATMs") and 255 cash recycler machines ("CRMs") as of March 31, 2022. As of March 31, 2022, its deposits and advances portfolio in the state of Tamil Nadu has contributed 75.06% to the Total Business. TMBL also focus on diversifying its growth in other high growth regions of India which will help increase its network and client base. Other than Tamil Nadu, it is present in 15 other states and 4 union territories of India. Apart from Tamil Nadu, it has sizable presence in the states of Maharashtra, Gujarat, Karnataka, and Andhra Pradesh with presence across 90 branches and 125 ATMs and 18 CRMs as of March 31, 2022. TMBL has also been consistently growing its customer base from, approximately 4.66 million as of March 31, 2020 to approximately 4.91 million as of March 31, 2021 to approximately 5.08 million as of March 31, 2022 at the CAGR of 4.36% from Fiscal 2020 to 2022. It has built a strong portfolio of advances and deposits across its customer base.

Advances: Bank's advances portfolio primarily consists of lending to (a) Retail customers; (b) agricultural customers and (c) MSMEs ("RAM").

MSMEs: TMBL primarily offer various loan products to its MSME customers operating in manufacturing, trading and services sector. During the Fiscals 2020, 2021 and 2022 MSMEs contributed 37.92%, 39.08% and 37.38% respectively to its total advances with a CAGR of 8.55% from March 31, 2020 to March 31, 2022.

Agricultural customers: TMBL primarily offers loan products to individual farmers, group of farmers and agricultural corporates. During the Fiscals 2020, 2021 and 2022 agricultural customers contributed 24.77%, 27.41% and 29.70% respectively to its total advances with a CAGR of 19.70% from March 31, 2020 to March 31, 2022.

Retail customers: It primarily offers home loans, personal loans, auto loans, educational loans as well as security backed loans of various types to its retail customers. During the Fiscals 2020, 2021 and 2022 retail customers contributed 19.27%, 20.60% and 20.39% respectively to the total advances with a CAGR of 12.46% from March 31, 2020 to March 31, 2022.

Corporate customers: TMBL offers various kinds of loans to corporates, in textiles and other industries, with its assortment of banking products and services including working capital, term financial, trade financial, structured finance services, foreign exchange business funding in domestic and foreign currencies.

As on March 31, 2022, TMBL had a network of 509 branches, 12 administrative offices, 1,141 ATMs, 282 CRMs, and 101 E-lobbies. Out of these 509 branches, 76 branches are in metropolitan areas, 80 branches are in urban areas, 247 branches are in semi-urban areas, and 106 branches are in rural areas. It has wide presence in south India and further diversifying its branches in other states of India, with 90 branches located in the states of Maharashtra, Gujarat, Karnataka and Andhra Pradesh respectively.

Objects of Issue:

Bank proposes to utilize the Net Proceeds towards augmenting its Tier–I capital base to meet its future capital requirements. Further, the Gross Proceeds from the Offer will also be used towards meeting the expenses in relation to the Offer. Additionally, Bank expects to receive the benefits of listing the Equity Shares on the Stock Exchanges.

Competitive Strengths

Strong legacy, loyal customer base and focus on improving servicing framework: With almost 100 years of history, TMBL has established itself as a well-recognized scheduled commercial bank having a strong network of branches, ATMs and CRMs across several states of South India including Tamil Nadu being its home state, along with Maharashtra, Gujarat, Karnataka, and Andhra Pradesh, which has enabled it to maintain a strong customer base. As of March 31, 2020, 2021 and 2022, TMBL had 4.66 million, 4.91 million and 5.08 million customers respectively with a CAGR of 4.36% from March 31, 2020 to March 31, 2022. Further, large portions of its existing customers have been associated with it for more than five years specifically in the states of Tamil Nadu, Andhra Pradesh, Maharashtra, Karnataka and Gujarat contributing 81.61%, 77.33%, 68.55%, 59.96% and 58.44% of its total customer base in each of these states respectively as of March 31, 2022, and 85.03%, 3.64%, 2.74%, 2.05% and 1.82% of its overall customer base as of March 31, 2022, across the 16 states and 4 union territories where it is present. Bank has consistently worked towards developing long-term relationships with its customers based on its knowledge of local needs and its experience in the sector, amongst other things. With a focus on increasing existing customer base, TMBL has introduced various alternate banking channels such as ATMs, CRMs, internet banking, mobile banking, E-Lobbies, point of sales (“PoS”), banking and debit and credit cards. It has also received several awards in recognition of its operations and loyal customer base over the years.

Strong presence in Tamil Nadu with focus to increase presence in other strategic regions: Since incorporation, TMBL has built a strong and trusted network of customers in the State of Tamil Nadu. As of March 31, 2020, 2021 and 2022 its deposits and advances in the state of Tamil Nadu contributed to 75.93%, 76.33% and 75.06%, respectively, of its Total Business. As of March 31, 2022, it had 4.32 million customers, 85.03% of its overall customer base, contributing to its deposits and advances portfolios in the State of Tamil Nadu. Tamil Nadu is also one of the fastest growing states, with continued focus on MSME and textile industry with GSVA at current prices growing at a CAGR of 11% over Fiscals 2017-2022 against the country wide growth of 9%. Tamil Nadu is under penetrated which presents an opportunity for further growth in GDP funded by bank loans. Recently, the state government of Tamil Nadu has also introduced various initiatives such as the Industrial Policy 2021 to achieve an annual growth rate of 15% in the manufacturing sector and the Tamil Nadu New Integrated Textile Policy, 2019, amongst others. Tamil Nadu and Gujarat’s deposits increased at 10% and 9% each in Fiscal 2022, whereas Maharashtra’s growth was at 15%. In terms of advances growth in Fiscal 2022, Gujarat displayed highest growth of 12%, followed by Tamil Nadu and Maharashtra which grew at 10% each.

Apart from TMBL’s home state, Tamil Nadu, it focuses on diversifying its reach in already existing network including in the states of Gujarat, Maharashtra, Karnataka and Andhra Pradesh. As of March 31, 2022, its businesses, including the deposits and advances portfolios, in the state of Tamil Nadu, Maharashtra, Andhra Pradesh, Karnataka and Gujarat contributed 75.06%, 5.78%, 3.67%, 3.47% and 2.91% to its Total Business. Its focus to increase markets share in these states more specifically in home state where TMBL is located across 369 branches, 949 ATMs, 255 CRMs, 91 E-Lobbies, 3,939 PoS as of March 31, 2022, has therefore, benefited it and will help to further enhance its customer base and increase business operations.

Advances with focus on MSME, agricultural and retail segments: TMBL has traditionally focused on small ticket size loan products to MSME customers, agricultural and retail customers for its growth. Its advances portfolio consists of a wide basket of retail finance and small ticket size MSME finance products. Its focus is on understanding the needs and expectation of its customers, particularly in the RAM space and adopting strategies to target these customer segments for its growth. It has dedicated marketing managers and agri-officers across its regional offices who specifically focus on growing the network of its existing MSME and agricultural customers. TMBL leverage its presence in semi-urban and rural regions where it is located to attract more customers in the RAM segment. It has structured loan products available to meet the financial requirements of its MSME customers, which aids in growing its MSME customer base across all places where it is currently present. Bank’s RAM business has consistently increased over the last three Fiscals from Rs.

231,427.36 million in Fiscal 2020 to Rs. 295,205.01 million in Fiscal 2022 at a CAGR of 12.94%. Its advances to the RAM segment represent 88.14% of its net advances as at March 31, 2022. In the development of a socially inclusive model, focusing on bringing in customers in the underserved sectors into the banking mainstream. Therefore, its focus has been to further enhance its RAM mix to help it gain more market share in Tamil Nadu and other regions where it continues to exist.

Consistently growing deposit base with focus on low-cost retail CASA: TMBL has adopted a customer-first approach, with an emphasis on customer relationships. Apart from the individual segment, it has focused on account sourcing on value based CASA products, have started following segmental approach on CASA growth by introducing segment wise CASA products such as Trust, Association, Society, Colleges, Charities ("TASC") and CASA accounts of central and state government schemes under its "TMB Savings for Government Segments" account. Its CASA portfolio is diversified and has low concentration with 2.91% of deposits from its top 20 deposit holders and 4.75% deposits from its top 50 depositors as of March 31, 2022. TMBL continuously strives to increase reliance for transactions on digital channels which are more cost effective than physical channels. Its digital banking channels enables a smooth transition from physical to digital usage and enhance customer experience, designed to grow its business and improve its margins.

Professionally managed Bank with experienced senior management team and board of directors: TMBL's Board of Directors comprises 11 directors and two nominee directors appointed by the RBI. The 11 directors include its Managing Director and Chief Executive Officer and ten Non-Executive directors, of whom six are Independent Directors, one of whom is a woman Director. They bring substantial experience and independent directors with diverse experience including sectors such as banking, law, business administration, other streams of finance such as accounting and auditing. Its senior management team's capabilities, reputation, extensive network of industry relationships, and wide ranging experience in the finance and banking industry is critical to its strategy to grow, modernise, and develop further. It typically recruits its senior management personnel with specialisation in areas such as investment, forex, risk management, treasury, agriculture, information technology, security, company secretaryship and law. It provides training programmes in a timely manner on areas such as, business skills, finance and resource management, human resource development, knowledge management, marketing, and information technology, which aims to enhance the technical, functional and soft skills of its employees. TMBL's experienced and high quality team of members throughout its organisation is instrumental in achieving customer trust and satisfaction.

Strong asset quality, underwriting practices and risk management policies and procedures: TMBL's strong customer understanding, focus on secured granular loan products and strong under-writing and risk management framework has helped it to maintain and further improve asset quality and driving its growth with consistent profitability. This is particularly important to it given its RAM portfolio focusing particularly on its MSME customers. Its focus on selective lending and limit its exposure to certain industries and sectors as a part of its strategy to monitor concentration risk. It has a Risk Management Committee to monitor its corporate customers on a monthly basis. It has a low customer concentration in terms of average ticket size. The average ticket size has remained in the range of 0.31 million to 0.34 million during the last three Fiscals. It has maintained its PCR at 87.92% as of March 31, 2022. Further, with an aim to maintain and improve its asset quality, it follows specific processes prior to loan approval and during the tenure of the loans depending on the ticket size of the loans. Its term loans are reviewed annually and higher value loans are reviewed periodically depending on the size of the loan products. This enables to Bank escalate any defaults at its regional offices in a timely manner. It also has a dedicated credit audit monitoring department which monitors its advances and helps avoid any downgrading in asset classification. TMBL also has recovery champions at specific branches, regional offices and its head office to enable it to maintain its asset quality.

TMBL also has early warning signals ("EWS") software to identify weaknesses in advances which is escalated to relevant officers and branches of the Bank. As of March 31, 2022, it has 59.46% of its outstanding loan value with less than 12 month tenures including working capital facilities renewable annually, 17.45% of its outstanding loan value with a tenure of 12-60 months and 23.09% with a tenure of more than 60 months. As of March 31, 2022, TMBL's average loan outstanding per branch is Rs. 663.03 million.

Consistent financial performance*:* TMBL's diversified portfolio, increasing market penetration across rural and semi-urban regions and focus on asset quality has enabled it to ensure consistent financial performance over the years. It also focusses on increasing its digital footprint which in turn has improved its operational processes that has reduced costs and resulted in improving the profitability of the Bank. It had the second highest Net Profit for Fiscal 2022 amongst its Peers, and its Return on Assets was also higher at 1.66% compared to a median 0.80% for its Peers for Fiscal 2022. In terms of a Return on Equity, TMBL had a ratio of 16.58% in Fiscal 2022, as compared to its Peers who reported a median of 8.30%. The ratio of CASA deposits to total deposits increased from 25.85% in Fiscal 2020 to 30.50% in Fiscal 2022 at a CAGR of 8.62%. Total advances of its Bank increased at a CAGR of 9.33% from Rs. 282,361.80 million in Fiscal 2020 to Rs. 337,481.69 million in Fiscal 2022.

Business Strategy:

Continue to strengthen product portfolios across deposits and advances: TMBL's growth in the past few years has been driven by strong understanding of the needs and expectations of its RAM customers. Its RAM Portfolio has increased from Rs. 231,427.36 million in Fiscal 2020 to Rs. 295,205.01 million in Fiscal 2022 at a CAGR of 12.94%. It has higher growth potentials in geographies where it exists such as in the State of Tamil Nadu and Gujarat which has lower bank credit to GDP ratios that are indicative of opportunities for banks and with its presence in the rural and semi-urban markets, TMBL is well positioned to continue attracting higher proportion of RAM customers. It will continuously focus on exploring and introducing new and customized fee-based products in connection with its centenary anniversary and strategies like TMB win-back campaign in addition to its existing products such as 'TMB Home Loan', 'TMB Affordable Home Loan', 'TMB Mahalir', and 'TMB Tractor'. It will also focus on improving experience of already available products as well as more tie ups with strategically identified third parties and leveraging its deep market expertise and relationships to leverage cross-selling opportunity, to grow deposits, improve advances sector wise and grow its fee-based income.

TMBL also aims to expand the branch-wise targets by opening new Retail Assets Central Processing Centres ("RACPCs") with dedicated home loan sales teams posted at these locations to drive further home loan portfolio growth. As of March 31, 2022, its Bank has one RACPC located at Chennai, Tamil Nadu, to which 36 branches of its Bank are linked. The housing loan portfolio of these 36 branches grew from 1,463 accounts with an outstanding amount of ₹ 2,900.79 million as on March 31, 2020 to 1,634 accounts with an outstanding amount of ₹ 3,405.53 million as on March 31, 2022. It is also focussed on diversifying its product portfolio so as to gain more customers and increase its market share. TMBL will continue to expand its relationship banking facilities to increase its network. It intends to focus more on fee based products such as issuing debit cards, credit cards, general insurance, life insurance, online bill payment services, depository services, government schemes, e-stamping and bill payments to its existing as well as new customers. It aims to identify potential clients in the import/export industry to augment its bill collection and forex transaction turnover. It also focuses on maximizing its revenue through its treasury operations to increase its profit on exchange, profit on sale of investments and income on investments.

Transformation through technology to improve efficiency and customer experience: The increased availability of internet access and connectivity across India requires a comprehensive technology-driven strategy to proactively develop new methods of reaching TMBL's customers and running its businesses. Its technology-driven strategy is focused on acquiring new customers by enhancing customer experience through its digital interfaces. Its technology focus is also intended to enhance its loan approval capabilities, reduce overall turnaround time, and facilitate maintaining and developing long-term customer relationships by allowing its customers to interact with it and access their accounts from the comfort of their personal space. It invests in technology as a means of improving its customers' experience, offering them a range of products tailored to their financial needs and making it easier for them to interact with it. TMBL constantly aims to upgrade its systems to match its customer demands and satisfy the needs of its diverse customer base.

Bank aims is to foster continued investment and innovation towards improved network security technology and architecture by adopting the "phygital" approach to sustainable and scalable growth. Its focus is on the simplicity of its products and services and its interface is designed for ease of use for all customers, including its customers in rural and semi-urban regions, supported by strengthened and automated backend processes. It continues to focus on creating efficient Management Information Systems ("MIS") and data analytics practices to monitor its portfolio and get actionable insights to help drive efficient decision making. It also continues to invest in its cyber security network and privacy protection systems, in order to supplement its growth and increase the robustness of its data security framework. TMBL's operational initiatives also provide it with insights into its customers, enabling it to cater to their needs in a customised manner.

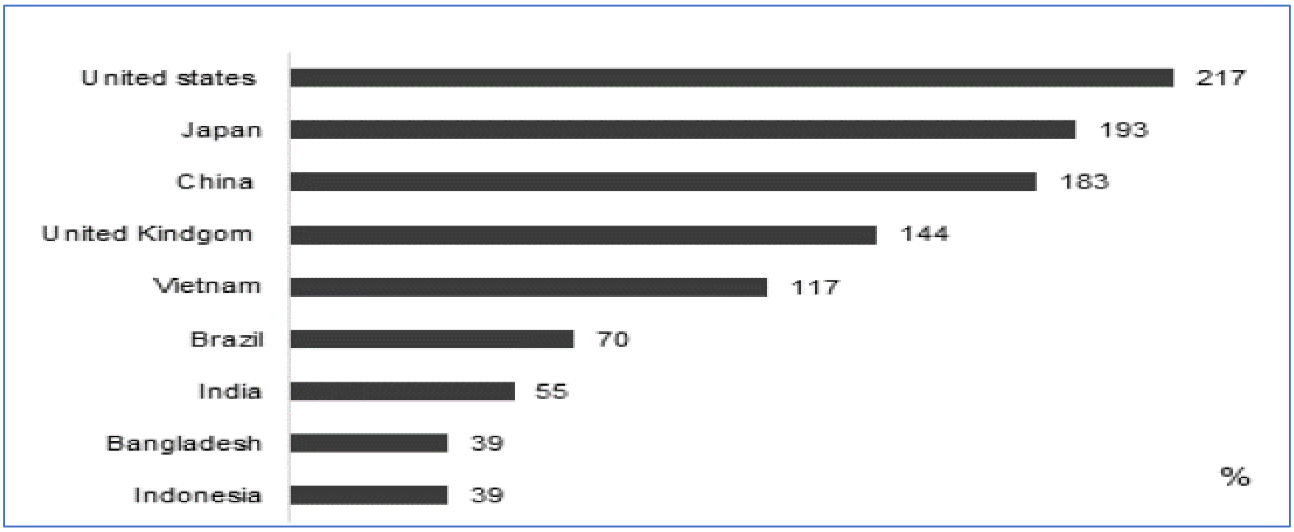
Continue to improve asset quality: TMBL aim is to continuously monitor and improve asset quality by focusing on secured advances, high loan to value ratio, diversification across loan book tenures, low concentration across branches and more stringent audit procedures for sanction of the loans specifically focusing on higher value loans. Its risk assessment, mitigation and management measures towards reducing NPAs and managing its stressed assets portfolio is particularly important to it, given its focus on its RAM portfolio. It also intends to reduce its NPAs by continuing to offer various schemes of settlement to address the issues specifically faced by small ticket borrowers. Further, it proposes to boost NPA recovery through one-time settlements, and monitoring of small value NPA accounts. TMBL will continue its focus on establishing and maintaining comprehensive strategies to achieve NPA targets by operating a dedicated credit recovery department and a region- wise cluster based oversight mechanism. It maintains provisions to account for any NPA and write offs including technical/prudential write-offs. At the same time, it aims to ensure that there is strict adherence to underwriting processes and standard operating procedures which are issued for each product offerings.

Industry:

Under-penetration of the Indian banking sector provides opportunities

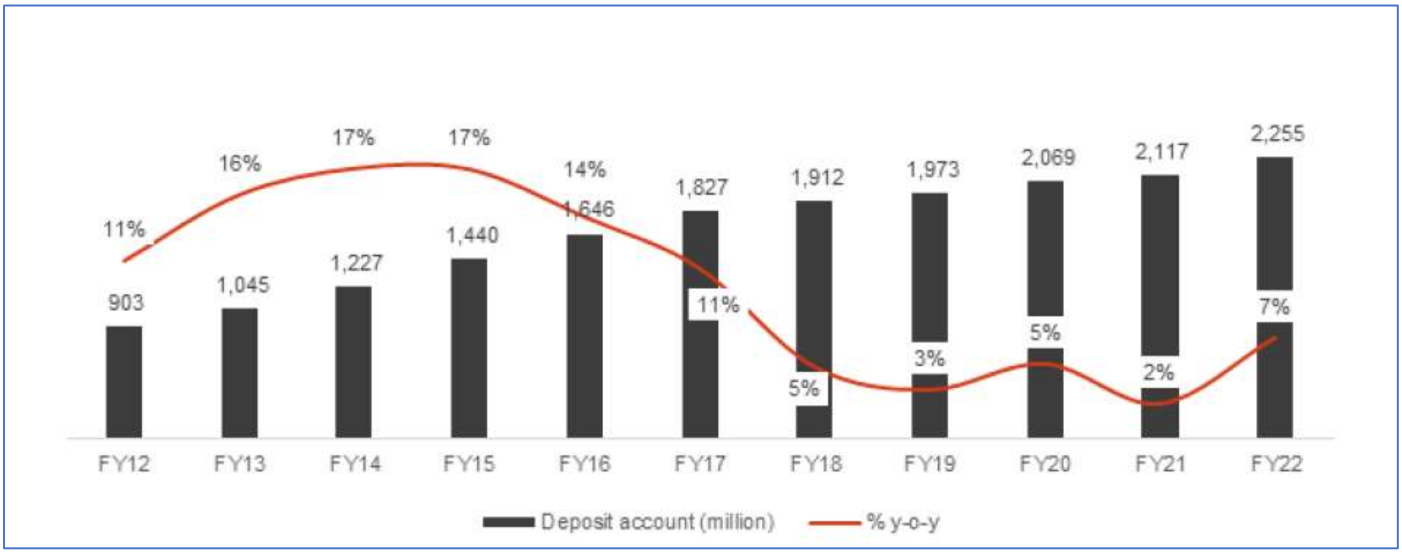
The Indian banking sector is significantly under-penetrated, which provides immense opportunities for banks and other financial institutions. The domestic bank credit-to-private sector as % to gross domestic product (GDP) stood at 55% as of 2020.

Domestic credit to private sector (% of GDP) as of 2020



Financial inclusion has been one of the key priorities of the government as well as banks over the past decade. Pradhan Mantri Jan Dhan Yojana (PMJDY), launched in August 2014, is aimed at ensuring affordable access to financial services — banking/savings and deposit accounts, remittances, credit, insurance, and pension. PMJDY focuses on household coverage, while the earlier schemes focused on coverage of villages. It aims to extend banking facilities to all within a reasonable distance in each sub-service area (consisting of 1,000-1,500 households) across India. As on March 31, 2022, 450 million PMJDY accounts had been opened; of these, 67% were in rural and semi-urban areas with aggregate deposit of Rs 1,665,000 million.

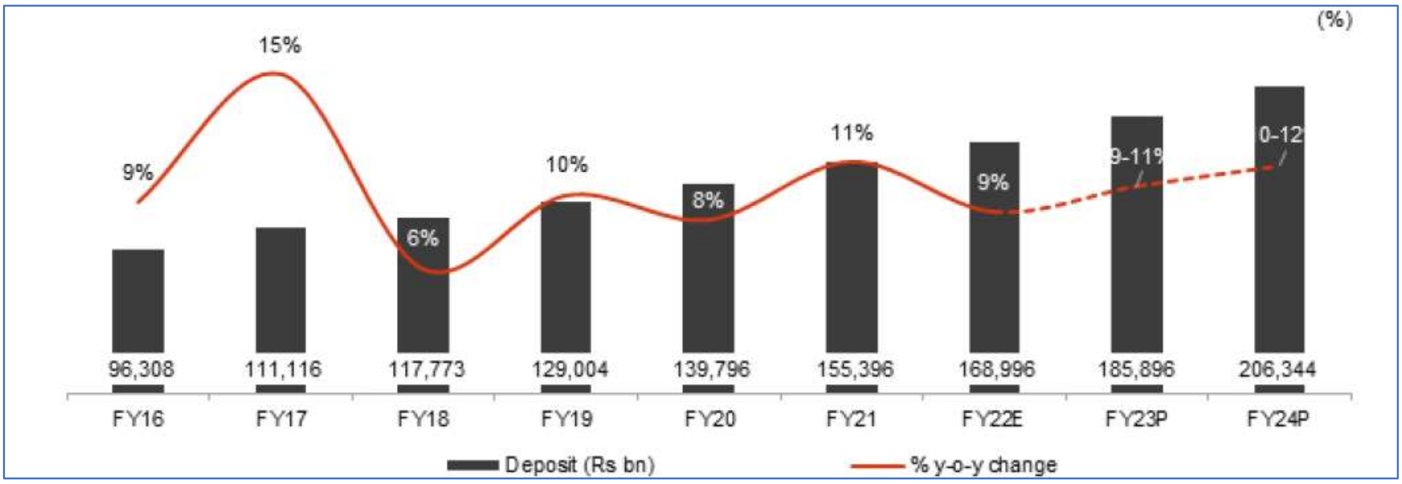
Growth in number of deposit accounts (including current, savings, term and others) in scheduled commercial Banks



Deposits to grow at a healthy rate of 9-11% during fiscal 2023

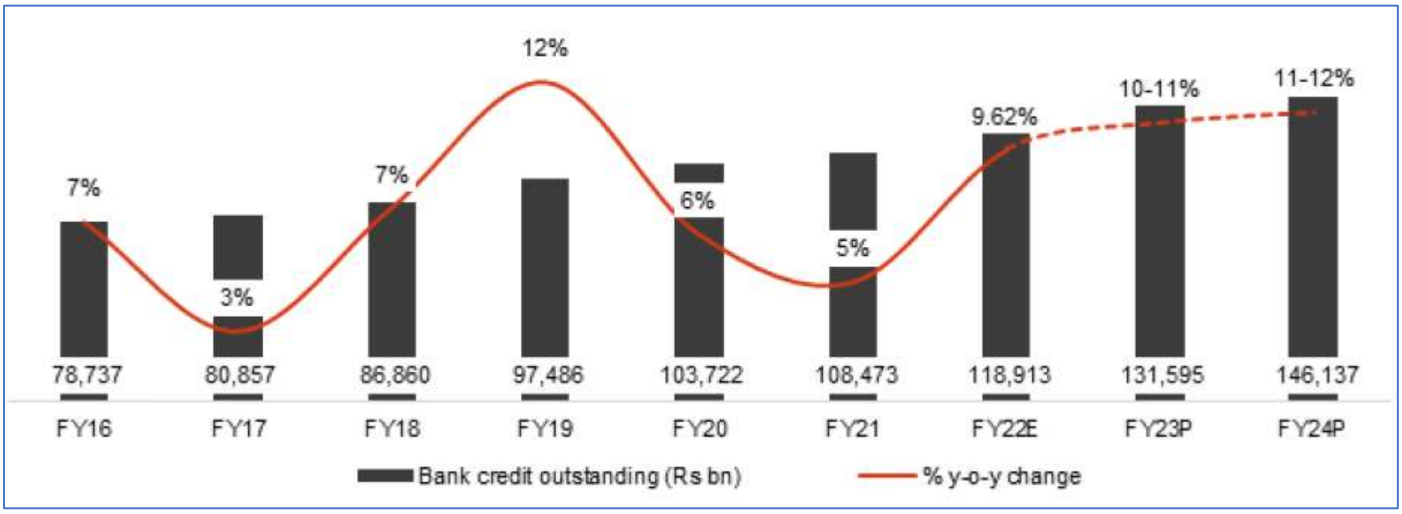
The banking sector enjoyed a healthy deposit compound annual growth rate (CAGR) of ~10% between fiscals 2016-21. With the outbreak of Covid-19 in fiscal 2021, conserving money became a priority and households reduced their private consumption, leading to 11% deposit growth in the fiscal. Further, the weighted-average domestic term deposit rate declined 80 basis points (bps) from 6.07% in April 2020 to 5.28% in March 2021. With the RBI keeping it stance accommodative and policy rates unchanged for the entire fiscal 2022, the weighted average term deposit rate declined a further 25 bps to 5.03% as of March 2022. During the monetary policy meeting in April 2022, the RBI signalled a gradual removal of the accommodative policy — it increased the policy repo rate by 40 bps in May 2022 and 50 bps in June 2022. CRISIL Research expects deposits to grow 9-11% during fiscal 2023, driven by an expected hike in policy rates by an additional 75 bps the fiscal, pushing the repo rate 50 bps above the pre-pandemic level by fiscal-end, and banks, in turn, transmitting the hike by increasing deposit rates.

Deposits (Rs billion) and % on-year change in India



Credit growth to continue at 10-11% during fiscal 2023

Bank credit outstanding and % on-year change



In fiscal 2021, the Indian economy witnessed the sharpest contraction since Independence, due to the onset of the pandemic and imposition of a nationwide lockdown. To help deal with the impact of the pandemic, the government and the RBI took several initiatives to provide relief to borrowers. While the impact was significant in the first half of fiscal 2021, faster-than-expected revival led to moderate credit growth of 4.6% in fiscal 2021. The most significant initiatives included the Rs 3,000,000 million (revised upwards to Rs 5,000,000 million) Emergency Credit Line Guarantee Scheme (ECLGS); provision of loan moratorium; and option of restructuring loans to corporates, micro, small and medium enterprises (MSMEs), and individual borrowers under the restructuring framework (One-time restructuring - OTR 1.0 and 2.0).

In the first half of fiscal 2022, the second wave of the pandemic forced both borrowers and lenders to tread cautiously, leading to muted growth in bank credit. Growth picked up in the third quarter of fiscal 2022, and with a mild third wave, the momentum continued in the fourth quarter supported by pent-up and festive season demand. Further, the amount sanctioned under the ECLGS aggregated to Rs 3,320,000 million and disbursement aggregated to Rs 2,590,000 million as of April 2022. The scheme has primarily aided the MSMEs to obtain credit from the banking sector and revive business activities. CRISIL Research expects bank credit to grow 10-11% during fiscal 2023, driven by the retail and agriculture segments and supported by recovery in services and industrial credit.

Private banks to continue to outpace public banks in credit growth in the medium term

Traditionally, public banks have accounted for the major proportion of the banking credit outstanding. However, low profitability, a weak capital position, low operational efficiency and an increase in stressed loans in the past few years led to slowdown in their loan growth. As a result, public banks gradually lost market share to private banks, which were relatively well capitalised and had a higher degree of operational efficiency. Public banks, which accounted for 71% share in credit outstanding in fiscal 2015, accounted for only 58% share in fiscal 2022. A partial economic slowdown resulted in lower credit growth in fiscal 2020 for both public and private banks. In fiscal 2021, growth for public banks stood at 5%, while private banks were able to grow 8% due to better capital buffers and increased focus on retail segment. Therefore, the latter gained further market share. As merged banks focus on integration and banks placed under corrective action come out of the PCA framework, credit growth of public banks is expected to lag that of private banks in the medium term. In fiscal 2022, private banks' focus on credit growth, especially in the retail segments, aided them to grow at a healthy double-digit rate of 14%. Growth at public banks also picked up to 7%. CRISIL Research expects credit growth of 8-10% at public banks and 14- 15% at private banks during fiscal 2023.

Merging banks: In fiscal 2019, public banks picked up growth because of improving asset quality and capital infusion by the government, which, in turn, improved the capital position of a number of banks and helped most PCA banks come out of the framework. Also, operational efficiency improved due to economies of scale after the SBI group merger (April 2017). After the merger of Bank of Baroda-Dena Bank-Vijaya Bank (April 2019), the Ministry of Finance announced the next round of public bank mergers by consolidating 10 banks into four banks (merging banks) with effect from April 1, 2020. These are Punjab National Bank with Oriental Bank of Commerce and United Bank, Union Bank of India with Corporation Bank and Andhra Bank, Canara Bank with Syndicate Bank, and Indian Bank with Allahabad Bank. This exercise of consolidating public banks aided in improving operating efficiency with economies of scale and is expected to help in speedier resolution of assets in the long run.

Gross non-performing assets (GNPA) of banks to improve to 5.4-5.6% in fiscal 2023

The pandemic resulted in one of the worst economic declines in decades. Airlines, hospitality, travel, gems and jewellery, auto dealers, and real estate were hit the hardest, given the discretionary nature of these sectors. Both collections and disbursements were impacted significantly in the first half of fiscal 2021. However, with measures taken by the government and the RBI assisting in containing the deterioration in asset quality, overall GNPA ended the fiscal at 7.4%.

The RBI announced a host of measures to enhance liquidity, ease financial market conditions, address cash flow concerns, and improve market sentiment following a near-halt in economic activity. The measures such as loan repayment moratorium provided relief to borrowers until August 2020 and loan restructuring framework helped customers who were financially impacted by the pandemic in the rest of fiscal 2021. These relief measures helped contain asset quality deterioration.

About 0.9% of the total credit outstanding was restructured as of March 2021 under the one-time restructuring framework (OTR 1.0), which was significantly lower than earlier estimates. In the case of public banks, the majority of the restructuring came from the corporate sector. In the case of large and mid-size private sector banks, the proportion of retail assets in total restructuring (invoked + implemented) was relatively high.

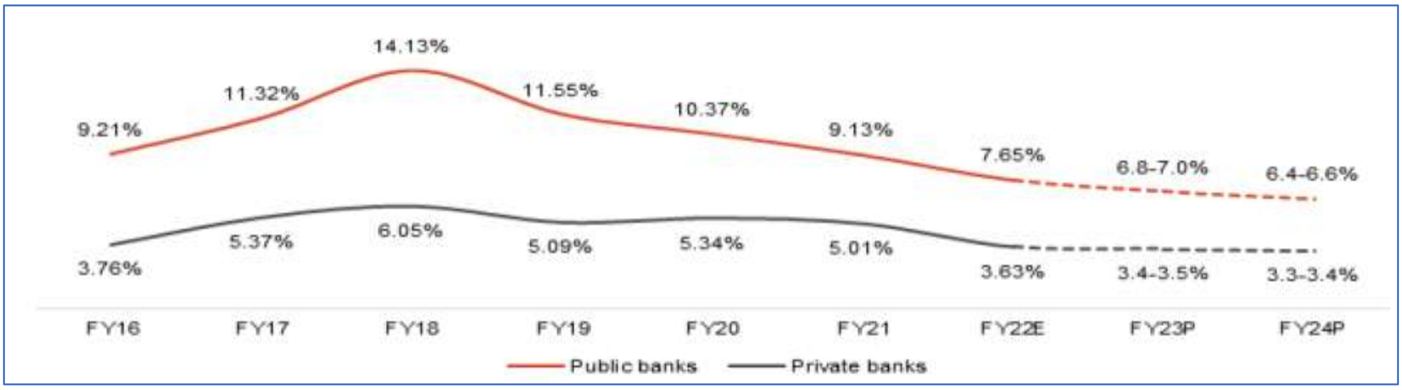
The RBI announced the restructuring framework (OTR 2.0) in May 2021, during the second wave of the pandemic. This framework saw better response from corporate borrowers —the window for application ended on September 30, 2021 (with the last date to implement the restructuring for banks being December 31, 2021). CRISIL Research estimates the overall restructuring (OTR 1.0 and 2.0) to have ranged between 1.50% and 1.80% of the loans outstanding as of March 2022.

Given the restructuring took place in fiscals 2021 and 2022 and the estimated tenure of the restructuring is around two years, CRISIL Research believes the behavior of such portfolios would be clear after fiscal 2023. GNPA of both private and public banks improved in fiscal 2022 on account of reduction in fresh slippages and improvement in upgrades and recoveries. GNPA of scheduled commercial banks stood at a six-year low of ~6% as of March 2022. CRISIL Research expects the bank's asset quality to improve further to 5.40-5.60% in fiscal 2023, primarily on account of lower slippages and expectation of recoveries via the NCLT and National Asset Reconstruction Company Ltd (NARCL) route.

GNPA of both public and private banks to improve this fiscal

GNPA of public banks started declining since 2019 due to resolution of stressed assets. As of March 2021, GNPA of these banks reduced almost 130 bps to 9.13% due to support from asset classification standstill, moratorium and restructuring. In case of private sector banks, the GNPAs have remained in range of 5-6% between fiscal 2017-21. And similar trend observed in public banks, the asset quality of private banks improved to 3.63% as of March 2022 with better recoveries across segment, especially, in industrial and agriculture segment. Further, the restructuring framework 2.0 announced in May 2021 on account of stress amid the second wave of the pandemic provided an option to stressed individual, corporate and MSME borrowers to restructure their loans. This along with an increase in credit guarantees under the ECLGS to Rs 5,000,000 million and the extension of ECLGS timelines to March 31, 2023, in the Union Budget 2022-23, has assisted in containing the deterioration of asset quality. CRISIL Research expects the momentum to continue this fiscal with improvement in asset quality across lenders.

GNPA of public and private banks (%)



The setting up of NARCL or the 'bad bank' will also help resolve the stressed asset scenario. Banks have finalised a loan of Rs 1,500,000 – 2,000,000 million, which is to be transferred to NARCL in a phased manner. Of this, about 15 bad-loan accounts aggregating to ~Rs. 500,000 million will be transferred in the first phase. However, recovery from these loan accounts is a key monitorable.

Product-wise

Agri-loans to increase at healthy pace in fiscal 2023

Loans outstanding for agriculture and allied activities (collectively agri-loans) in India logged 8% CAGR between fiscals 2016 and 2021, supported by a good monsoon and higher banking penetration. In fiscal 2018, though, farm loan waiver by many states led to a deceleration in growth to 4% on-year. But, in fiscal 2019, the pace picked up again to 8% over a low base amid banks' priority sector lending (PSL) targets and a normal monsoon. A normal monsoon in fiscal 2021 offset the impact of the pandemic as well. However, the pandemic affected allied activities such as horticulture and cash crops because of lower exports. Nevertheless, as of March 2021, agri-loans rose a sharp 10% on-year. In fiscal 2022, due to higher food-grain and horticulture production, elevated prices of crops such as cotton, and support from the agriculture fund, agri-credit grew ~10%, with loans outstanding of banks at Rs 14,613,489 million. CRISIL Research expects agri-credit to grow 11-13% during fiscal 2023, supported by PSL targets, expected higher food-grain production, an increase in commodity prices, and an increase in the agri-credit target to Rs 18,000,000 million this fiscal from Rs 16,500,000 million during fiscal 2022. Further, continued government focus on agri-allied sectors via schemes such as the agri-infrastructure fund and linking KCC to animal husbandry and fisheries will also support credit growth. GNPA of agri-loans surged to 10.14% in fiscal 2020. The pandemic had limited impact on the sector in fiscal 2021, with GNPA range-bound at 9.80%. In fiscal 2022, GNPA declined to 9.40%, owing to initiatives such as one-time settlement of loans by SBI. Further, an increase in profits has supported farmers in repaying loans on time. CRISIL Research expects asset quality to improve ~50 bps on-year this fiscal on expectations of a normal monsoon and higher on-year profitability in kharif crops

Industrial credit to continue growing in fiscals 2023 and 2024

Credit to industry witnessed muted or a marginal growth at 1% CAGR between fiscals 2016 and 2021 owing to asset quality concerns. However, it rose sharply in fiscal 2019, led by lending to the infrastructure segment. In fiscal 2021, though, credit growth weakened as most underlying sectors, such as chemicals, engineering, and construction, were significantly affected amid demand challenges heaped by the pandemic, with credit outstanding in several sectors declining 6-8% on-year. In fiscal 2022, industry credit grew ~8% supported by the textile, construction, engineering and food processing segments and partially offset by de-growth in the basic metals and metal products segment on account of an increase in metal prices, which helped companies generate higher revenues and, in turn, deleverage balance sheets during the last two fiscals. CRISIL Research expects the recovery in industrial credit to continue, with growth in a range of 8-10% during fiscals 2023 and 2024.The government's Production-Linked Incentive scheme, which is a concerted push to drive manufacturing with greater focus on large employment-generating and export-oriented sectors, is a positive for industry and is likely to aid credit growth over the medium term. GNPA for industrial credit declined in fiscal 2021, due to the resolution of stressed assets via NCLT and the restructuring framework 1.0. Further, the RBI's announcement of the restructuring framework 2.0 in May 2021, during the second wave of the pandemic, provided stressed corporate and MSME borrowers with an option to restructure their loans. Lower slippages from large corporate accounts, higher recovery or write-offs, and lower credit costs helped improve asset quality.

Credit growth in services segment to remain range- bound

Credit to the services segment logged 12% CAGR between fiscals 2016-21, driven by lending to NBFCs which registered 18% CAGR. Credit growth to the NBFC segment was muted during fiscal 2021 due to the onset of the pandemic, which affected the country's economy, and stressed assets in certain non-bank segments. Given that one-third of the services sector lending in the bank portfolio is towards NBFCs, portfolio quality and credit growth of underlying NBFC assets are also a key monitorable. NBFC credit has grown at 18% CAGR from fiscals 2016-21. However, post the muted credit growth in fiscal 2021, lenders were cautious in funding NBFCs owing to asset quality concerns. Hence, credit growth in lending to NBFCs was at ~11% in fiscal 2022 on account of a lower base coupled with banks cautiously extending credit to NBFCs serving less stressed segments. Services segment credit is estimated to grow 8-10% on-year during fiscals 2023 and 2024, driven by lending towards the NBFC and trade segments. The RBI's ECLGS incentive helped in revival of this sector from pandemic-induced stress. As of April 2022, loans sanctioned under this scheme crossed Rs 3,320,000 million (of total Rs 5,000,000 million), with ~66% of the guarantees issued (as % of loans sanctioned).

The Covid-19 disruption, lockdowns and sluggish economic activity significantly affected the services sectors, such as transport operators, tourism, hospitality, and trade. Since the government provided one-time restructuring schemes 1.0 and 2.0 in August 2020 and May 2021, respectively, ECLGS to MSMEs, this helped improve the asset-quality in fiscal 2022 to 5.80%. CRISIL Research expects the services sector GNPA to at 5.50-5.70% in fiscal 2023 and 5.30-5.50% in fiscal 2024.

Retail segment to continue healthy double-digit growth in fiscal 2023 and 2024

Banking credit to the retail segment recorded 15% CAGR between fiscals 2016 and 2021. However, during the first half of fiscal 2021, retail loan exposure of banks to the housing and auto segments declined due to the pandemic. Nevertheless, it picked up faster than expected in the second half, helping post healthy credit growth of 11% by fiscal 2021-end. The growth was driven by improved affordability on account of low interest rates and stamp duty cuts announced by state governments in retail housing segments. With the RBI keeping its stance accommodative during fiscal 2022, interest rates for housing loans continued to be at a historical low during fiscal 2022 (starting from 6.50%). This helped retail housing and overall retail credit grow at 13% on year. Further, despite an expected increase in property prices and policy rates rising by an additional 75 bps over 90 bps in first quarter of this fiscal, overall affordability is likely to remain favorable. Given this and healthy momentum in housing demand, CRISIL Research expects housing credit to grow at 14-16% in fiscal 2023. Credit to the overall retail segment is expected to lead the growth of the banking sector, increasing at 13-15% on year fiscals 2023 and 14-16% on-year during 2024 supported by healthy growth in housing, consumer durable, gold and other personal loans segments. GNPA of retail loans was at 1.80% in fiscal 2020. Because of the Covid-19 fallout and deterioration in asset quality in the segment, GNPA increased to 2.10% as of March 2021. GNPA spiked further in the first quarter of fiscal 2022 due to the second wave. However, loan restructuring under the one-time restructuring 2.0 announced by the RBI in May 2021 contained further deterioration. Improvement in economic activities and the mild third wave in the fourth quarter also helped, pushing the GNPA back to pre-Covid levels at 1.80% as of fiscal 2022.

Retail housing loans to witness healthy double-digit credit growth in fiscal 2023

Home loans outstanding of banks was Rs 16,844,240 million as of March 2022, almost double the figure five years ago. The segment recorded a healthy 14% CAGR over fiscals 2016-21. However, in fiscal 2021, the pace slowed, led by moderation in credit growth following the pandemic. Large-scale migration of labour back to their hometowns / villages during the nationwide lockdown, and subsequent uncertainty regarding project execution, affected buyer sentiment for under-construction projects. Also, incomes were impacted, especially in the first half of fiscal 2021. However, there was a faster-than-envisaged revival in the second half of fiscal 2021, with the RBI, along with the Centre and state governments, providing impetus. In the case of housing / real estate, demand, which had touched a low during the lockdown, revived faster than expected in the second half, since:

Real estate developers offered discounts and/or freebies Maharashtra and Karnataka cut stamp duty on real estate Moratorium and one-time restructuring (OTR 1.0 and 2.0) offered under the RBI's Resolution Framework for borrowers under stress due to pandemic Banks and non-banks slashed housing loan interest rates to historical lows

Vehicle loans segment to rise 9-10% in fiscal 2023

Vehicle loans outstanding of banks was Rs 4,026,675 million as of March 2022, with the segment posting a healthy 8% CAGR over fiscals 2016 to 2021. Demand had taken a hit in fiscal 2021 and had remained muted for few segments in fiscal 2022 as well, due to the stress induced by the two Covid-19 waves. Credit growth in fiscal 2023 will be supported by the continued rise in vehicle prices, healthy offtake from the domestic front and the easing chip shortage which will ensure the industry to post healthy growth. On asset front, it expects pickup in vehicles sales volumes and improved loans-to-value (LTVs) across segments in this fiscal, resulting in overall disbursement growing by 14-16%. In return, CRISIL Research expects the vehicle loan book to grow by 9-10% in fiscal 2023.

MSMEs credit to grow at a healthy rate of 11-13% during fiscal 2023

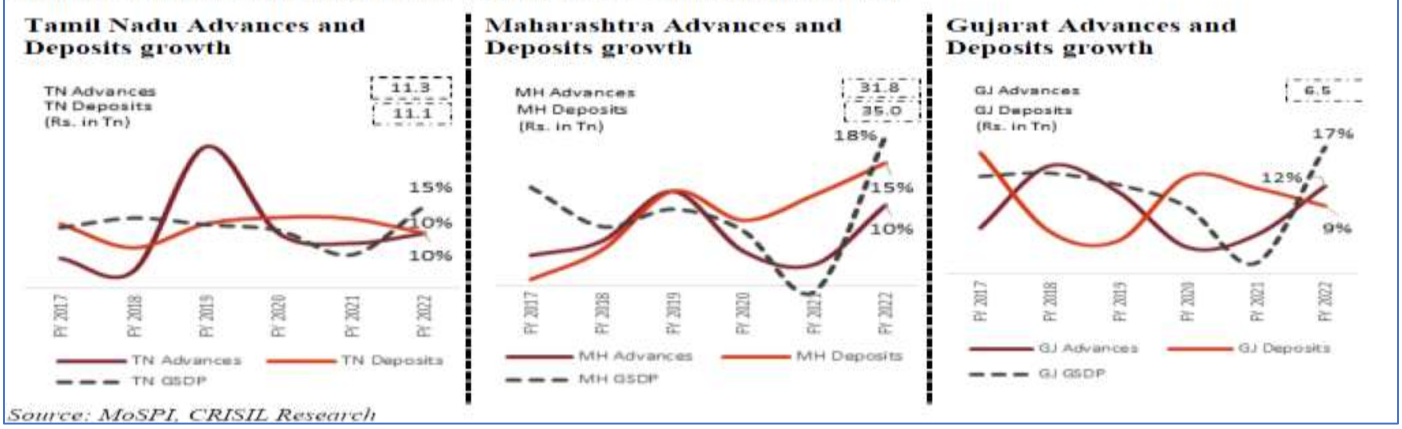
As per the revised definition, a firm with investments under Rs 500 million and turnover under Rs 2500 million is called an MSME. The first and second waves in fiscal 2021 and the first quarter of fiscal 2022, respectively, hit the segment hard. With the sectors close linkage to economic activities, the magnitude of the impact was significant due to frequent lockdowns and restrictions, which affected demand and supply, and hence profitability across most sectors. This necessitated relief measures, which were promptly announced by the government in the form of the ECLGS in fiscal 2021, which was reviewed on a timely basis to reduce impact on the sector. However, most of the disbursements under the scheme were by banks (among which private-sector banks showed greater proclivity than public-sector banks for utilising ECLGS), leading to credit growth of 8% in fiscal 2021. The second wave impacted the MSME segment again, leading to muted growth in the first half of fiscal 2022 on account of disruption in business activity due to localised lockdowns. With the hit to the economy in the first quarter, the government extended the ECLGS, then ending in June 2021, to September 2021 (currently extended till March 31, 2023). This supported the sector to revive from degrowth in the first quarter of fiscal 2022, with banks posting a sequential growth in their MSME book at the end of the second quarter. Revival of economic activity, strong export and domestic support, coupled with a mild third wave, helped banking MSME credit clock healthy double-digit growth of 15% during fiscal 2022. CRISIL Research expects banks to continue credit growth at 11-13% in fiscal 2023.

Banking in Tamil Nadu

Increased savings has a direct impact on lending capabilities and overall GDP growth

Increased deposits with banks act a low-cost source of funds for the bank's lending activities. This allows the bank to charge a comparatively low rate of Interest, and hence, passing on cost benefit to the borrower. This borrowing allows businesses to borrow for growth and expansion, thereby boosting economic growth and GDP. There appears to be a positive correlation between GDP, advances and deposits for the state. Tamil Nadu's and Gujarat's deposits increased at 10% and 9% respectively in fiscal 2022, whereas Maharashtra's growth was 600 bps higher at 15%. In terms of advances growth in fiscal 2022, Gujarat displayed highest growth, i.e.,12%, followed by Tamil Nadu and Maharashtra which grew at 10% each.

Advances and deposits growth mirrors the GSDP trend till fiscal 2021



Source: MoSPI, CRISIL Research

Lower bank credit-to-GDP ratio indicates potential for further lending in the state

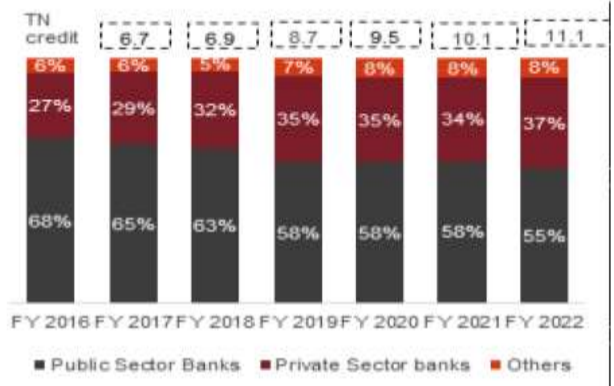
Tamil Nadu is under-penetrated, which presents an opportunity for further growth in GDP funded by bank loans. Its bank credit to GDP stood at 52% compared with ~100% in case Maharashtra and 33% for Gujarat during fiscal 2022.

Public sector banks dominate the state's lending portfolio

Tamil Nadu's bank credit had been increasing at a faster pace compared with All India Credit till fiscal 2021. In fiscal 2022, the state's bank credit increased 10% as against All India Credit, which rose 11%. Public sector banks accounted for 55% of total funding; down from 68% in fiscal 2016. On the other hand, private banks have been gaining share.

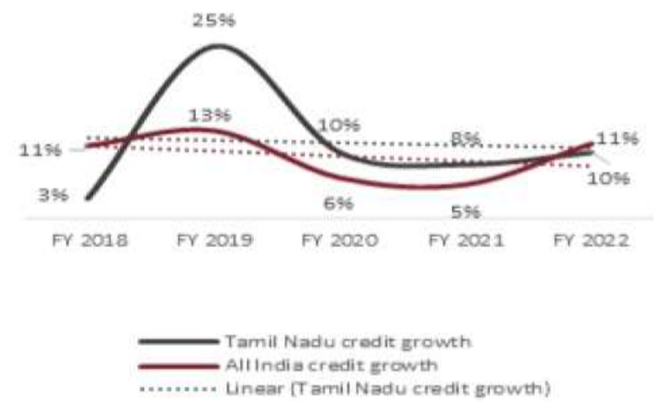
Public banks contribute majority in Tamil Nadu's lending mix

(Rs. In Tn)



Note: Others include foreign and small finance banks
Source: RBI

Average growth over the last 5 years is in line with all India credit



Source: RBI

In fiscal 2022, retail (housing, vehicle, education and other personal loans) accounted for ~25% of the overall credit, followed by industry (24%), agriculture (21%), and services (17%). By sector, credit to agriculture has grown at a robust rate thanks to various government initiatives and schemes. Notably, growth has been higher compared with the all-India growth in agricultural credit. Retail has also been growing at a steady rate.

Mirroring the trend of advances, public sector holds majority share in deposits as well, though reducing every year

Deposits with banks in Tamil Nadu rose increase of 11% in fiscal 2022 over fiscal 2021. Public sector banks hold the majority share (~55%) at present, though private banks have been gaining share over the past few years because of the attractive rate of interest offered by them.

Key Concerns

- 37.73% of its paid-up equity share capital or 53.76 million Equity Shares are subject to outstanding legal proceedings which are pending at various forums and, in connection with which, proceedings against the Bank have been initiated by various regulatory authorities, including the RBI, the Directorate of Enforcement, some of whom have imposed and sought to impose penalties on it in the past.
- Business, reputation and financial results could be impacted by adverse results in legal proceedings. TMBL has also issued notices and initiated various recovery proceedings against defaulting borrowers under the SARFAESI Act and failure by such borrowers to repay the outstanding borrowings pursuant to such notices and proceedings may adversely affect the business.
- Received and may in the future receive multiple anonymous whistle blower complaints, which may adversely affect its reputation which could consequently adversely impact the business, financial condition and results of operation.
- Its former director has filed a writ petition before the High Court of Madras seeking to prevent the Bank from undertaking the Offer.
- TMBL has regional concentration in southern India, especially Tamil Nadu. Any adverse change in the economic, political, or geographical conditions of Tamil Nadu and other states in which it operates can impact its results of operations.
- Bank is subject to stringent regulatory requirements and prudential norms and its inability to comply with such laws, regulations and norms may have an adverse effect on its business, results of operations, financial condition and cash flows.
- TMBL's contingent liabilities exceed its net worth, which, if they materialize, may adversely affect its results of operations, financial condition and cash flows.
- TMBL is subject to supervision and inspection by authorities such as the RBI.
- The COVID-19 pandemic has had and may continue to have certain adverse effects on business, operations, cash flows and financial condition and the continuing impacts of COVID-19 are unpredictable and cannot be predicted.
- TMBL has had negative cash flows in the past and may continue to have negative cash flows in the future.
- TMBL is required to maintain CRR and SLR and capital adequacy ratios and any increase in these requirements could materially and adversely affect the business, financial condition, and results of operations.

- Bank will be unable to open new branches unless it is listed and are also required to obtain prior permission from the RBI to open new branches.
- The majority of the business premises are leased. Accordingly, TMBL is exposed to risks typical to leasing of commercial real estate, including risk of being required to relocate certain of its premises from time to time.
- TMBL depends on the accuracy and completeness of information about customers and counterparties. Its financial condition and results of operations could be negatively affected by relying on financial statements of customers that do not comply with generally accepted accounting principles or on other information that is incorrect or materially misleading.
- TMBL is dependent on its Key Managerial Personnel and the loss of, or its inability to attract or retain, such persons could adversely affect the business, financial condition, results of operations and cash flows.
- TMBL undertakes fee based activities and its financial performance may be adversely affected by an inability to generate income from such activities.
- Any non-compliance with mandatory AML, KYC and CFT laws and regulations could expose TMBL to liability and harm its business and reputation.
- If TMBL is unable to manage its large network or implement its growth strategies, its operations may suffer and performance may be adversely affected.
- TMBL is currently significantly dependent on Retail, MSME and Agri-financing, customers and any adverse developments in these segments could adversely affect the business, results of operations, financial condition and cash flows.
- An increase in portfolio of NPAs may materially and adversely affect the business and results of operations.
- TMBL may not be able to maintain or grow its CASA ratio in accordance with its strategy, which may result in higher cost of funds, and which may materially affect the financial condition and results of operations.
- Business comprises both traditional general banking activities and micro banking activities that exposes TMBL business overall to the risks faced by each sector, which may negatively impact its performance.
- TMBL is required to lend a minimum percentage of its Adjusted Net Bank Credit (“ANBC”) to certain priority sectors. Any adverse performance by such priority sectors or any change in the RBI’s regulations relating to priority sector lending or its Bank’s inability to meet the priority sector lending targets could attract punitive action from the regulator which may have an adverse impact.
- Business is vulnerable to interest rate related risks. Volatility in interest rates could adversely affect the net interest margin, the value of its fixed income portfolio, its security receipts, its income from treasury operations, the quality of loan portfolio, and financial performance.
- An inability to obtain, renew or maintain statutory and regulatory permits and approvals required to operate business may adversely affect the business, financial condition, results of operation and cash flows.
- Industry is very competitive and growth strategy depends on the ability to compete effectively.
- Risk management measures may not be fully effective in mitigating risks in all market environments or against all types of risks, which may adversely affect the business and financial performance.
- TMBL may face cyber threats attempting to exploit its network to disrupt products and support services to customers and/ or theft of sensitive internal data or customer information, which may cause damage to its reputation and adversely affect the business and financial performance.
- The RBI may remove any employee, managerial personnel or may supersede Bank’s Board of Directors in certain circumstances, which may materially affect the Bank’s business, results of operations, and financial conditions.
- Depends on brand recognition, and failure to maintain and enhance awareness of the brand would adversely affect ability to retain and expand its base of customers.
- Political, economic or other factors that are beyond control may have an adverse effect on the business, results of operations, financial condition and cash flows.
- Changing laws, rules and regulations and legal uncertainties, including adverse application of corporate and tax laws, may adversely affect the business, prospects and results of operations.
- Any downgrading of India’s debt rating by an international rating agency could have a negative impact on the business and financial performance.
- Financial instability in other countries may cause increased volatility in Indian financial markets which could harm the business, its future financial performance, and the prices of the Equity Shares.

Profit & Loss

Particulars (Rs in million)	FY22	FY21	FY20
INCOME			
Interest earned	38338.6	36090.5	34661.1
Other Income	8225.8	6443.5	5264.2
TOTAL	**46564.4**	**42534.0**	**39925.3**
EXPENDITURE			
Interest Expended	20,186.3	20,715.3	21,465.9
Operating Expenses	11,110.4	9,796.5	8,509.1
Provisions & Contingencies	7048.6	5988.9	5873.3
TOTAL	**38,345.3**	**36,500.7**	**35,848.4**
Net Profit for the year	**8219.1**	**6033.3**	**4076.9**
EPS	57.7	42.3	28.6
FV	10	10	10

Balance Sheet

Particulars (Rs in million) As at	FY22	FY21	FY20
CAPITAL & LIABILITIES			
Capital	1,425.1	1,425.1	1,425.1
Reserves & Surplus	51,932.0	44,374.7	38,371.4
Deposits	449,331.2	409,704.2	368,250.3
Borrowings	0.0	0.0	3,240.0
Other Liabilities and Provisions	25,896.7	19,767.7	16,301.2
TOTAL	**528,584.9**	**475,271.7**	**427,588.0**
ASSETS			
Cash and balances with Reserve Bank of India	21,131.1	16,802.9	14,144.1
Balances with Banks and Money at Call and Short Notice	17,388.9	10,247.9	23,221.5
Investments	130,354.6	117,032.1	94,673.3
Advances	334,915.4	310,696.0	277,157.6
Fixed Assets	2,108.4	1,371.8	1,284.5
Other Assets	22,686.4	19,121.1	17,107.0
TOTAL	**528,584.9**	**475,271.7**	**427,588.0**
Contingent Liabilities	87,977.0	113,870.8	73,096.2
Bills for Collection	9,831.4	8,959.2	7,975.0

(Source: RHP)

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