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06.10.2022

Madam / Dear Sir,

Sub: State Bank of India – Rating by Fitch Ratings

Pursuant to Regulation 30 and other applicable provisions of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, we enclose the rating update issued by Fitch who has affirmed SBI rating at 'BBB-' with outlook stable.

Please take the above information on record and arrange for dissemination.

Yours faithfully,

(Sham K.)
AGM (Compliance & Company Secretary)



RATING ACTION COMMENTARY

Fitch Affirms State Bank of India at 'BBB-'; Outlook Stable

Tue 04 Oct, 2022 - 7:29 AM ET

Fitch Ratings - Singapore/Mumbai - 04 Oct 2022: Fitch Ratings has affirmed State Bank of India's (SBI) Long-Term Issuer Default Rating (IDR) at 'BBB-'. The Outlook is Stable. The agency has also affirmed the bank's Viability Rating (VR) at 'bb' and its Government Support Rating (GSR) of 'bbb-'. A full list of rating actions is below.

KEY RATING DRIVERS

Support-Driven IDR: The Long-Term IDR on SBI are support-driven, with the GSR above the bank's VR, which is the highest among Indian state banks.

High Systemic Importance: SBI's GSR is the same as India's sovereign rating (BBB-/Stable), and reflects Fitch's view that the probability of extraordinary state support is the highest for SBI among Indian banks due to its high systemic importance as the largest Indian bank, the state's 56.9% controlling ownership, and its broader policy role than peers. The Stable Outlook on the IDR mirrors the Outlook on the sovereign IDR.

Stable Operating Environment: Fitch expects India's strong potential GDP growth of 7% over the medium term and stable operating environment, despite some near-term inflationary pressures, to create moderate opportunities for banks to do profitable business. Our view is further aided by India's large and diversified economy, high domestic consumption growth, and reasonable insulation from external risks.

Dominant Presence: We have assessed SBI's business profile score at 'bbb-'. The score is the highest among Indian banks and above the operating environment score of 'bb'. SBI is India's largest bank by a wide margin with shares of more than 20% of system assets, liabilities and deposits, as it benefits from better pricing power and unparalleled domestic reach. SBI leads most state-owned peers on digitisation, with a focus on business and productivity gains amid stiff competition.

Traditional Model; Government Influence: SBI's business model is traditional, with loans forming 58% of assets, but government influence can weigh on its business model, but even more so its risk appetite, similar to other state banks. Fitch believes the bank's appetite for risk was previously higher than is typical for a bank with its market position, which, in a less-benign environment, has exacerbated the negative impact on key financial metrics.

Growth Gradually Returning: SBI's guidance of loan growth of over 15% in the financial year ending March 2023 (FY23) highlights that growth appetite is gradually returning across segments, amid an economic recovery. We expect the retail business to remain the key growth driver, with the bank showing cautious optimism towards corporate and SME segments as interest rates rise. The bank is more focused on credit quality as its moderate capitalisation compels it to optimise capital utilisation.

Impaired Loans to Improve: We expect SBI's impaired-loan ratio to continue to improve in FY23 (1QFY23: 3.9%), supported by lower fresh impaired loans and ongoing recoveries. A more meaningful unwinding of relief loans will likely test this trend in FY24, but loan impairment charges will likely remain below 1%, provided there are no negative shocks from this pool of stressed Covid-19-affected loans. Specific provision cover on legacy impaired loans is 75% while overdue loans (between 30-90 days) are limited at 0.24%.

Strengthening Core Profitability: We have revised the earnings and profitability score to 'bb-/stable' as we expect the four-year average operating profit/risk-weighted assets (RWAs) to exceed 1.25% by FYE23 (1QFY23: 1.3%) despite the negative impact of rising interest rates on bond valuation in the near term. However, the expected benefits for earnings from higher net interest margin (1QFY23: 2.9%) and lower loan impairment charges (1QFY23: 0.6%), will remain the primary drivers of profitability over the foreseeable future once the near-term effects of rising interest rates play out on treasury income.

Modest Capital Buffers: SBI's common equity Tier 1 (CET1) ratio is being tightly managed, leaving only a modest buffer above the required minimum of 8.6%, given the higher growth

likely in 2023 and 2024. It was around 10% at 1QFY23 after factoring in profits, the same level as FY22.

The decline in the net impaired loans/CET1 ratio (FY22: 11.4%) has eased risk to capital, but SBI's prior appetite for risk and legacy loans, in particular, have rendered it prone to cyclical performance swings, such that capital remains vulnerable to future shocks. That said, we view SBI as best placed among state banks to access any necessary additional core capital, whether through the capital markets or via its state shareholder.

Deposits Dominate Funding: We assessed the funding and liquidity score at 'bbb-/stable, the same as the sovereign rating. The loan/customer deposit ratio inched up to 71.7% by end-1QFY23 (per preliminary disclosures) from 69.8% at FYE22, and will likely settle at higher and normalised levels as loan growth gains momentum. The share of customer deposits in total funding remains high at 90% at end-1QFY23 due to high depositor confidence in SBI, but there could be some shift from low-cost deposits to term deposits in the near term.

Balance-sheet liquidity is robust, while overall funding and liquidity remains a strength of SBI's intrinsic credit profile. That said, the bank, like others in India, remains exposed directly and indirectly to the sovereign.

RATING SENSITIVITIES

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

IDR AND GOVERNMENT SUPPORT RATING

The GSR is most sensitive to Fitch's assessment of the government's propensity and ability to support SBI, based on the bank's size, systemic importance and linkage to the state. Weakening of the government's ability to provide extraordinary support - reflected by negative action on India's sovereign ratings - would lead to similar action on the Long-Term IDR.

Negative action on the Long-Term IDR is also likely should Fitch perceive any reduction in the government's propensity to extend timely support, in which case the agency will reassess the GSR, and the bank's Long-Term IDR, although that is not our base case.

VIABILITY RATING

Fitch views SBI's VR - which reflects a moderate degree of financial strength - to be reasonably stable in the near term, but it could be downgraded if there is significant deterioration in the operating environment, or if a heightened risk profile were to become a more binding constraint on the bank's moderate capital buffers.

These could manifest through a weakening in all of the following key financial metrics, assuming our assessment of business profile remains unchanged:

- drop in SBI's CET1 ratio below 10%, irrespective of its capital fungibility and flexibility, and without a credible plan to restore it to closer to the 'bb' CET1 ratio threshold of 12%; alongside
- four-year average impaired-loan ratio significantly exceeding 5%; and
- four-year average operating profit/RWA ratio being sustained below 1.25%.

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

IDRS AND GOVERNMENT SUPPORT RATING

Positive sovereign rating action would lead to corresponding changes to SBI's Long-Term IDR, provided the sovereign's propensity to support remains unchanged. An upgrade to SBI's GSR is more probable in the event of a sovereign upgrade than for the other large state banks, even though Fitch views the government's ability and propensity to support those banks as high due to their systemic importance and history of support. SBI is significantly larger than the others and it has a broader quasi-policy role, which makes it strategically important to the state. However, an upgrade of the sovereign rating appears unlikely in the near term.

VIABILITY RATING

A VR upgrade appears unlikely in the near term, in light of the prevailing uncertainties and risks to the bank's intrinsic profile. Nevertheless, an upgrade could stem from a faster-than-expected and sustained economic recovery supporting a higher assessment of the operating environment - particularly if it propels the bank's asset quality and capitalisation towards a path of sustainable improvement.

These could manifest through the stronger key financial metrics listed below:

- SBI sustaining a four-year average impaired-loan ratio well below 5%;
- fresh equity injection that supports the accumulation and sustaining of capital buffers to levels well above 12%.

At the same time, evidence that SBI can sustain recent reductions in its risk appetite and demonstrate an ability to generate stronger earnings without compromising its risk profile could be positive for the bank's overall VR.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

The bank's medium-term note programme and senior notes are rated at the same level as the Long-Term IDR, in line with Fitch's criteria. The notes constitute direct, unsubordinated and unsecured obligations of the banks, and rank equally with all their other unsecured and unsubordinated obligations.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

SBI's programme rating and senior debt rating will move in tandem with the IDR. Both ratings would be downgraded if the Long-Term IDR is downgraded. They would also be upgraded in the event the IDR is upgraded, though we view this to be unlikely in the near term.

VR ADJUSTMENTS

The operating environment score of 'bb' is above the implied category of 'b' for the following adjustment reasons: economic performance, and size and structure of the economy (positive).

The asset-quality score of 'bb-' is above the implied category of 'b' for the following adjustment reason: historical and future metrics (positive).

The earnings and profitability score of 'bb-' is above the implied category of 'b' for the following adjustment reason: historical and future metrics (positive).

The capitalisation and leverage score of 'bb-' is above the implied category of 'b' for the following adjustment reason: capital flexibility and ordinary support (positive).

The funding and liquidity score of 'bbb-' is above the implied category of 'bb' for the following reason: deposit structure (positive).

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

SBI's IDRs and Outlook are the same as India's sovereign ratings and directly linked via the bank's GSR, which reflects our view of the probability of extraordinary state support, should there be a need.

ESG CONSIDERATIONS

SBI has an ESG Relevance Score of '4' for Governance Structure, in line with similarly rated state banks. This reflects our assessment that key governance aspects, in particular, board independence and effectiveness, ownership concentration and protection of creditor and stakeholder rights, are of moderate influence, yet are negative for SBI's credit profile, and are relevant to the ratings in conjunction with other factors.

Similar to other Indian state banks, Fitch views SBI's governance to be less developed, as evident from significant lending to higher-risk borrowers and segments, which has led to above-average levels of impaired loans and credit losses. The board is also dominated by government appointees and the bank's business models often focus on supporting government policy, while it already has a healthy appetite for risk. Lending could be directed towards socioeconomic and economic policies, which may include lending to government-owned companies. These factors also drive our view of the bank's state linkages, which influence support prospects and drive the long-term ratings.

SBI has an ESG Relevance Score of '4' for Financial Transparency. This reflects our assessment that the quality and frequency of financial reporting and the auditing process are of moderate influence, yet are negative for SBI's credit profile, and are relevant to the ratings in conjunction with other factors.

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 divergence 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, although we expect SBI to be reasonably better placed among peers. Still, we regard financial transparency as 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 ↕
State Bank of India	LT IDR	BBB- Rating Outlook Stable		BBB- Rating Outlook Stable
	Affirmed			
	ST IDR	F3	Affirmed	F3
	Viability	bb	Affirmed	bb
	Government Support	bbb-	Affirmed	bbb-

senior unsecured	LT	BBB-	Affirmed	BBB-
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senior unsecured	LT	BBB-	Affirmed	BBB-
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[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

[Bank Rating Criteria \(pub. 08 Sep 2022\) \(including rating assumption sensitivity\)](#)

ADDITIONAL DISCLOSURES

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State Bank of India

EU Endorsed, UK Endorsed

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Banks Asia-Pacific India
