

Utkarsh Small Finance Bank Limited^(Revised)

August 13, 2025

Instruments	Amount (₹ crore)	Rating ¹	Rating Action
Tier-II Bonds	15.00	CARE A; Stable	Downgraded from CARE A+; Negative
Tier-II Bonds	200.00	CARE A; Stable	Downgraded from CARE A+; Negative

Details of instruments in Annexure-1.

Rationale and key rating drivers

The downgrade of the long-term rating of Utkarsh Small Finance Bank Limited (USFBL) reflects the continued stress in its micro-banking segment, which constituted a dominant 47% of the total advance's portfolio as on June 30, 2025. The bank's asset quality and profitability deteriorated in Q1FY26 due to elevated credit costs and interest income reversals. While the pressure on asset quality and profitability is expected to continue in the near term, CARE Ratings Limited (CareEdge Ratings) notes that the bank has plans to raise funds up to ₹750 crore by September 2025, a timely execution of which would be necessary to maintain adequate capitalisation levels and absorb potential asset quality stress, and hence, would be a key monitorable.

USFBL's gross non-performing assets (GNPA) ratio deteriorated significantly to 11.42% as on June 30, 2025, from 2.78% a year earlier reflecting elevated slippages in the micro-banking portfolio. The increase in slippages in Q1FY26 was further exacerbated by the new regulatory framework introduced under MFIN 2.0 and is expected to persist through FY26. Net NPA (NNPA) to net worth ratio also declined sharply to 35.21% as on June 30, 2025 from 1.42% as on June 30, 2024.

In terms of business growth, the bank has recalibrated its micro-banking disbursements in light of the heightened stress. While overall advances growth moderated in FY25 and Q1FY26, USFBL has strategically pivoted towards secured lending. As a result, the micro-banking share in the portfolio declined from 62% as on March 31, 2024 to 47% as on June 30, 2025, while the share of secured loans increased from 34% to 45% over the same period. While the shift is expected to improve bank's portfolio quality, it is likely to exert pressure on profit margins due to the relatively lower yields on secured lending products.

On the liabilities front, while the bank has successfully expanded its deposit base in recent years with significant growth in deposits, its current account savings account (CASA) ratio remains relatively low at 19.64% as on June 30, 2025. The rating also considers comfortable liquidity coverage ratio of 239% as on June 30, 2025, providing adequate liquidity cushion.

CareEdge Ratings will closely monitor the bank's asset quality trends and profitability trajectory in FY26. The bank's ability to contain further slippages, improve collection efficiency, and earnings momentum while strengthening its secured lending base and maintaining adequate capitalisation will be key rating sensitivities going forward.

Rating sensitivities: Factors likely to lead to rating actions
Positive factors: Factors that could individually or collectively lead to positive rating actions/upgrade:

- Sustained improvement in asset quality and profitability while maintaining comfortable capitalisation levels.
- Improvement in profitability metrics with return on total assets (ROTA) above 1.5% on a sustained basis
- Diversification in resource profile with continuous improvement in CASA proportion on a sustained basis.

Negative factors: Factors that could individually or collectively lead to negative rating actions/downgrade:

- Deteriorating capitalisation with overall capital adequacy ratio (CAR) going below 18%.
- Sustained deterioration in asset quality, profitability, and liquidity.

Analytical approach: Standalone

Outlook: Stable

The stable outlook is on the expectation that the increased capital post equity raise will help bank maintain adequate capitalisation despite near-term pressures on profitability and asset quality.

¹Complete definition of ratings assigned are available at www.careratings.com and other CARE Ratings Limited's publications.

Detailed description of key rating drivers:

Key strengths

Adequate, although declining, capitalisation levels

The bank continues to be adequately capitalised by maintaining sufficient cushion over the minimum regulatory requirement of 15% (Tier-I: 7.5%). However, CareEdge Ratings notes that USFBL's capitalisation level moderated in Q1FY26 with capital adequacy ratio (CAR) at 19.64% and Tier-I at 16.71% as on June 30, 2025 from 20.93% and 17.88%, respectively, as on March 31, 2025. The bank is in the process of raising upto ₹750 crore by H1FY26. The equity raise will aid in maintaining capital buffers to support growth while providing for the deterioration in the asset quality. Any delay in raising the additional capital could weaken the capitalisation profile in case of a continued asset quality deterioration in the micro-banking book, and hence remains a key rating monitorable.

Continued diversification of loanbook

Advances growth moderated in FY25 and Q1FY26, primarily as the bank is calibrating its micro-banking disbursements following stricter regulatory guardrails and sectoral stress while continuing strong growth in non-micro-banking retail segments and improving the advances mix in favour of secured portfolio. The bank registered 2.3% growth in the gross loan portfolio year-on-year and stood at ₹19,224 crore as on June 30, 2025, while the micro-banking segment de-grew by 20%. The largest segment of the portfolio continues to be micro-banking loans; though its share has reported a decline from 62% of the loan book as on March 31, 2024 to 47% as on June 30, 2025 (49% including Business Correspondence). While the bank will continue to grow micro-banking loans, it is focusing on increasing other non-micro banking segments, especially secured loans, whose proportion increased from 34% as on March 31, 2024 to 45% as on June 30, 2025. Going forward, other lending verticals (being smaller in size) are expected to grow even faster than micro-banking business and hence the share of micro-banking loans in overall loan book is expected to reduce further. The reduction in micro finance loan book and reduction in the geographical concentration remain key rating monitorable.

Key weaknesses

Deterioration of asset quality and profitability

USFBL's asset quality deteriorated materially in FY25 and Q1FY26, with the GNPA rising to 11.42% as on June 30, 2025 (March 31, 2025: 9.43%, March 31, 2024: 2.51%), and the NNPA to net worth ratio increasing sharply to 35.21% (March 31, 2025: 31.67%, March 31, 2024: 0.16%), which is relatively higher than the peers. This was primarily due to slippages in the micro-banking segment, which accounted for a sizable portion of the loan book. As on June 30, 2025, the bank's provision coverage ratio (PCR) on GNPA's stood at 59%, which is comparatively lower than that of peer small finance banks. CareEdge Ratings notes that the X-bucket collection efficiency, which improved in Q4FY25 compared to previous quarter, deteriorated in Q1FY26 due to implementation of MFIN Guardrail 2.0 from April 1, 2025.

The bank reported net loss of ₹239 crore for Q1FY26 compared to profit after tax (PAT) of ₹24 crore in FY25 (FY24: ₹498 crore), affected by high credit costs and interest reversals. Going forward, profit margins are expected to remain under pressure for FY26 due to continued stress in the microfinance sector and change in product mix in favour of lower yielding secured loans.

The bank's ability to manage asset quality and credit costs remains critical for stability of its profitability and return ratios going forward.

Geographical concentration of loan portfolio

The bank has 1,099 banking outlets spread across 27 states and union territories (UTs) as on June 30, 2025. The top two states - Bihar and UP, constituted ~46% of branches and 48% of gross loan portfolio (over 70% of microbanking loans) as on June 30, 2025. However, the geographical concentration is improving gradually with the opening of new branches outside of these two states.

The share of micro-banking loans in the loan book remained dominant at 47% as on June 30, 2025 (49% including Business Correspondence), which exposes the bank to inherent risks associated with the industry such as socio-political intervention, regulatory uncertainties, and challenges of unsecured lending.

Relatively low CASA

The bank's liability mix has undergone substantial change as deposits as a percentage of total liabilities has been increasing with reduction in dependence on borrowings, which is evident from the improving credit to deposit ratio. USFBL's deposits have grown 18% y-o-y and stood at ₹21,489 crore with CASA proportion remaining relatively modest at 19.68% as on June 30, 2025. The bank's CASA proportion remains lower compared to its peers in the small finance banking industry. The bank has been focusing

on building its granular retail deposits book and its CASA plus retail term deposits (upto ₹3 crore) constituted 74% of total deposits as on June 30, 2025. Its dependence on wholesale term deposits remained high at 26%, although the same has been improving in the last few years. CareEdge Ratings expects the bank to focus on raising CASA deposits, which would provide the bank a stable depositor base and reduce cost of funding over the medium term.

Liquidity: Strong

Per the structural liquidity statement as on June 30, 2025, there were no negative cumulative mismatches for time buckets up to one year. The bank also maintained surplus liquidity of ~₹3,900 crore over and above regulatory requirements, which provides liquidity buffer. In addition, the bank has access to borrowing from Reserve Bank of India's (RBI's) liquidity adjustment facility (LAF) and marginal standing facility (MSF) and option to refinance from Small Industries Development Bank of India (SIDBI), National Housing Bank (NHB), and National Bank for Agriculture and Rural Development (NABARD) among others, and access to call money markets. The bank's liquidity coverage ratio was comfortable at 239% as on June 30, 2025, against the minimum regulatory requirement of 100%.

Environment, social, and governance (ESG) risks

Given USFBL's service-oriented nature of business, its direct exposure to environmental risks remains low. However, it faces implicit environmental risks through its portfolio of assets. The bank has targeted reduction in energy consumption, preserve water quality, and availability in addition to plantation of trees. Customer data privacy and security remain the key social risk-related vulnerabilities for USFBL as breaches could attract regulatory attention and damage the bank's reputation. While digital banking offers many benefits to the bank, poor execution of IT strategies and failure to adequately meet customer needs could lead to high costs. On a positive note, USFBL is enhancing financial inclusion by offering products and services aimed at marginalised sections of society, addressing social concerns. Prudent lending to these underserved segments could create growth opportunities, which must be weighed in the context of asset quality risks, including borrower creditworthiness, economic vulnerabilities, and regulatory uncertainties. USFBL's Board comprises eight Directors, of which four are Independent Directors, including two female Directors.

Applicable criteria

[Definition of Default](#)

[Rating Outlook and Rating Watch](#)

[Banks](#)

[Financial Ratios - Financial Sector](#)

[Rating Basel III - Hybrid Capital Instruments issued by Banks](#)

About the company and industry

Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Financial services	Financial services	Banks	Other bank

Based out of Varanasi, USFBL is a subsidiary of Utkarsh CoreInvest Limited (UCL), a non-banking financial company non-deposit taking systemically important core investment company (NBFC-NDSI-CIC) with the RBI. The company commenced banking operations on January 23, 2017, upon receipt of license from RBI on November 25, 2016, and subsequent transfer of business from UCL, which was carrying on the micro lending operations since September 2009. USFBL extends micro-banking loans based on the joint liability group (JLG) model to individuals, which constituted nearly 50% of the gross loan portfolio of the company as on March 31, 2025. The bank also extends wholesale loans, MSME loans, and housing loans to the borrowers. USFBL provides micro-banking loans through Business Correspondence activities as well. As on June 30, 2025, it had 1,099 banking outlets, 362 ATMs, and 777 micro-ATMs. The bank is headed by Govind Singh, MD and CEO, whose reappointment as MD and CEO has been approved by RBI for three years on September 21, 2024.

USFBL, vide announcement to the stock exchanges on September 20, 2024, informed the exchanges that its board of directors approved scheme of amalgamation of UCL, the holding company with USFBL, subject to the approval of shareholders, debenture holders, RBI, Stock exchanges, National Company Law Tribunal (NCLT) and other competent authority, as may be applicable. The scheme is subject to the expiry of the lock-in restriction on equity shares held by UCL in the USFBL, which expires on January 19, 2025. The amalgamation would be through share exchange ratio of 669 equity shares of face value of ₹10 each of USFBL,

for every 100 equity shares of face value of ₹10 each of UCL. The Scheme would result in increase of public shareholding in USFBL from 30.98% as on June 30, 2024 to 100%. The Bank has received no-objection from RBI, BSE Limited and National Stock Exchange of India Limited on January 02, 2025, July 04, 2025, and July 07, 2025, respectively, to proceed with the approval of NCLT and other relevant statutory authorities, ensuring compliance with certain conditions / procedural matters in this regard.

USFBL Financials

Brief Financials (₹ crore)	31-03-2024 (A)	31-03-2025 (A)	Q1FY26 (UA)
Total income	3,579	4,365	1,019
PAT	498	24	-239
Total assets	23,798	28,010	27,677
Net NPA (%)	0.03	4.84	5.00
ROTA (%)	2.32	0.09	-3.44

A: Audited; UA: Unaudited; Note: these are latest available financial results

All calculations per CareEdge Ratings

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Detailed explanation of covenants of rated instrument / facility: Annexure-3

Complexity level of instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Bonds-Tier-II Bonds	INE735W08020	31-Aug-2018	10.58	30-Aug-2025	15.00	CARE A; Stable
Bonds-Tier-II Bonds	INE735W08061	27-Nov-2024	10.90	27-Nov-2031	105.00	CARE A; Stable
Bonds-Tier-II Bonds	Proposed	-	-	-	95.00	CARE A; Stable

Annexure-2: Rating history for last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2025-2026	Date(s) and Rating(s) assigned in 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023
1	Bonds-Tier-II Bonds	LT	-	-	-	-	-	1)Withdrawn (29-Sep-22)
2	Bonds	LT	15.00	CARE A; Stable	1)CARE A+; Negative	1)CARE A+; Stable	1)CARE A+; Stable	1)CARE A; Positive (29-Sep-22)

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2025-2026	Date(s) and Rating(s) assigned in 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023
					(12-Jun-25)	(31-Oct-24) 2)CARE A+; Stable (24-Sep-24)	(26-Sep-23)	
3	Bonds	LT	200.00	CARE A; Stable	1)CARE A+; Negative (12-Jun-25)	1)CARE A+; Stable (31-Oct-24)	-	-

LT: Long term; ST: Short term; LT/ST: Long term/Short term

Annexure-3: Detailed explanation of covenants of rated instruments/facilities: Not applicable

Annexure-4: Complexity level of instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Bonds-Tier-II Bonds	Complex

Annexure-5: Lender details: Not applicable

Note on complexity levels of rated instruments: CareEdge Ratings has classified instruments rated by it based on complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for clarifications.

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