India Ratings & Research
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India Ratings Upgrades Jammu and Kashmir Bank to 'IND AA-'/Stable

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India Ratings and Research (Ind-Ra) has upgraded Jammu and Kashmir Bank Limited's (JK Bank) Long-Term Issuer Rating to 'IND AA-' from 'IND A+'. The Outlook is Stable. The instrument-wise rating actions are as follows:

Details of Instruments

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (billion)	Rating assigned along with Outlook/Watch	Rating Action
Long-Term Issuer Rating	-	-	-	-	IND AA-/Stable	Upgraded
Basel III compliant Tier II bonds*	-	-	-	INR40	IND AA-/Stable	Upgraded

*Details in annexure

Analytical Approach

Ind-Ra continues to take a fully consolidated view of JK Bank and its wholly-owned subsidiary, JKB Financial Services Ltd., in its analysis to arrive at the ratings.

Detailed Rationale of the Rating Action

The upgrade reflects an increase in the capital buffers of the bank in FY24 in line with Ind- Ra's expectations, and continued improvement in the profitability profile of the bank, supported by the improving business socio- political environment in the union territory of Jammu, Kashmir & Ladakh (UTJKL) that has been aiding tourism, agriculture and small businesses. The rating continues to reflect the strong market position and franchise of the bank in the UTJKL territory.

List of Key Rating Drivers

Strengths

- Systemic importance
- Strengthened capital buffers
- Prospective asset quality metrics likely to be benign
- Reasonable deposit profile, with high proportion of current account saving account (CASA) deposits
- Improved profitability profile likely to sustain

Weaknesses

- Inherent geographic concentration

Detailed Description of Key Rating Drivers

Systemic Importance: Although it has a smaller scale compared to other peer banks, the bank remains systemically important, given its strong franchise and substantial market share in the UTJKL. The bank continues to be designated as the agent bank by the Reserve Bank of India for UTJKL. The bank has received continued financial support from the government of UTJKL. Considering JK Bank is a dominant bank in the strategically important and socio-politically sensitive union territories, it is of high systemic importance and plays a major role in the state economy. While this support had been present when the regions were administered by the state of Jammu & Kashmir, the bank's capital levels had been precariously close to the regulatory levels, given the loan concentration and higher dependence on the government for timely and adequate infusion than most centre-owned mainstream scheduled commercial banks. However, the capital levels have increased due to capital infusion, improving internal accruals and qualified Institutional placement.

Ind-Ra expects continued financial support from the UTJKL government (equity infusions; FY23: nil; FY22: INR5.0 billion, FY20: INR5.0 billion, FY17-FY18: INR5.3 billion) in a timely and adequate manner; these regions are governed by the central government since they are union territories. UTJKL continued to hold majority share of around 59% in the bank at FYE24.

Strengthened Capital Buffers: The CET1 ratio of the bank improved to 12% in FY24 (FY23: 11.05%; FY22: 10.35%), supported by qualified institutional placement of INR7.5 billion in FY24 and improved internal accruals, and is now better placed than historical levels. The increase in CET1 was partly offset by an increase in risk weighted assets (RWA) for unsecured retail loans during the year. However, this needs to be viewed in context of the bank's net non-performing assets (NPAs) being reduced to about 0.8% at FYE24 from 2.9% at FYE21. Also, in FY24, the tier 1 and overall CAR ratio of the bank improved to 13.1% (FY23: 12.3%, FY22: 11.7%) and 15.3% (15.4%, 13.2%). Furthermore, Ind-Ra believes the existing capital buffers are adequately placed to also absorb asset quality shocks.

Prospective Asset Quality Metrics Likely to be Benign: The asset quality metrics continue to improve, with gross NPAs of the bank declining further to 3.9% at 1QFYE25 (FYE24: 4.1%; FYE23: 6.0%; FYE22: 8.7%), and net NPAs falling to 0.8% (1.6%, 2.5%; 2.9%) in line with peer banks. The steady decline in NPA ratios could be also attributed to the improving business socio-political environment in the J&K territory that has been aiding tourism, agriculture and small businesses. The bank's provision coverage ratio declined slightly but remained strong at 81.1% in 1QFY25 (FY24: 81.4%, FY23: 74.4%, FY22: 73.2%), which is higher than that of peer banks. The bank continued to have a high special mention accounts (SMA) portfolio in FY24, with the share of SMA 1 and 2 portfolio remaining high at 7.2% of the total advances as of March 2024 (6.5% as of March 2023), compared to peer banks. However, the bank also maintains contingent provisions of around INR6 billion, indicating a conservative provisioning policy. The bank has taken various steps to reduce the SMA portfolio and the agency expects it to come down substantially by FYE25. In the near-to-medium term, the asset quality metrics are likely to remain benign in line with the operating environment.

Reasonable Deposit Profile, with High Proportion of CASA deposits: At 1QFYE25, the bank's CASA ratio declined but remained higher than peers at 49.8% (FY24: 50.5%, FY23: 54.1%; FY22: 56.6%, FY21: 56.9%), with the credit to deposit ratio remaining comfortable at 71% (FY24: 69.6%, FY23: 67.4%). JK Bank's CASA ratio is better than that of most peers due to the majority government ownership and it being the agency bank for UTJKL; this has helped JK Bank sustain traction in retail deposits over the years, as all the transactions related to the UTJKL government and government employees (salaries) are routed through the bank. Overall, the bank's deposit profile plays an important role in maintaining its margins (FY24:4.2%; FY23: 4.2%; FY22:3.7%). The cost of deposits, which stood at 4.4% in FY24 (FY23: 3.8%; FY22: 3.65%, FYE21: 4.10%), is one of the lowest rates among Indian scheduled commercial banks, implying lower-than-peers' deposit costs. However, the deposit profile remains constrained by limited deposit franchise outside UTJKL, as more than 89% of the deposits come from the territory.

Improved Profitability Profile likely to Sustain: The bank has been able to maintain slightly high net interest margins compared to peers at around 3.86% in 4QFY24 (4QFY23: 3.94%), mainly supported by the low cost of deposits. JK Bank had witnessed a loss of INR11.4 billion in FY20, with credit costs of 4.1%, but it subsequently turned profitable due to a continued decline in the credit costs (FY24: down 0.2%; FY23: 0.0%; FY22: 0.4%; FY21: 1.6%). The bank reported return on assets (RoA) of 1.18% in FY24 (FY23: 0.87%; FY22: 0.4%; FY21: 0.38%). The bank's profit increased to INR17.7 billion in FY24 (FY23: INR11.97 billion; FY22: INR5.02 billion) and stood at INR4.1 billion in 1QFY25. Ind-Ra expects the bank's credit costs to remain low in FY25 as well. Furthermore, the bank expects continued recoveries from the written-off assets in FY25 (FY24: INR1 billion; FY23: INR2 billion). The bank's cost to income ratio improved but remained high at 62.2% in FY24 (FY23: 66.2%, FY22: 71.4%) compared to peers. The bank has also been taking several initiatives for reducing its overall cost, which should augur well for its performance in the long term and targets to bring down the cost to income ratio to 50%-55%. Overall, Ind-Ra expects the profitability to sustain and further improve in the near-to-medium term, with likely RoA of 1.2%-1.3%.

Inherent Geographic Concentration: The geographical concentration declined slightly but remained high in FY24, with

UTJKL accounting for around 68.5% of the total portfolio (FY23: 69.8%, FY22: 72.5%), and around 89% of the deposits coming from this region. The management of the bank expects to gradually bring down the portfolio concentration to 60% by FY28, which remains to be seen. The concentration could be partly mitigated by the fact that around INR225 billion of the advances (24% of the overall portfolio) comprises retail loans to government employees, which is also guaranteed by the government of UTJKL. Also, the retail portfolio of the bank has seen limited delinquencies, with GNPAs remaining less than 0.5% historically.

Liquidity

Adequate: As per the bank's structural liquidity statement as of March 2024, the bank had a negative cumulative mismatch (outflows exceeding inflows) of around 9% of the total assets (INR37.8 billion) in the up-to-one-year bucket. However, this is adequately covered by the excess SLR of INR71.9 billion maintained by the bank as of March 2024. Moreover, it had a liquidity coverage ratio of 135% at 1QFYE25, against the regulatory requirement of 100%.

Rating Sensitivities

Positive: The bank's ability to reduce the geographical concentration in the J&K region in line with Ind-Ra's expectations and improve its market share, especially outside UTJKL, further improvement in the capital ratios and stable profitability from the core lending operations and the absence of any material deterioration in the asset quality could lead to a positive rating action.

Negative: Events that could, individually or collectively, lead to a negative rating action are as follows:
- any significant findings that come to Ind-Ra's notice that could have a material impact on the bank's financials or any deterioration in the bank's operating performance,
- decline in the bank's franchisee
- larger-than-expected asset quality issues, leading to a decline in the CET 1 ratio below 10% on a sustained basis.

ESG Issues

ESG Factors Minimally Relevant to Rating: Unless otherwise disclosed in this section, the ESG issues are credit neutral or have only a minimal credit impact on JK Bank, due to either their nature other way in which they are being managed by the entity. For more information on Ind-Ra's ESG Relevance Disclosures, please click here. For answers to frequently asked questions regarding ESG Relevance Disclosures and their impact on ratings, please click here.

About the Company

Srinagar-based JK Bank was established in 1938. It is majority-owned (59% as of March 2024) by the government of UTJKL. The bank had 1,006 branches and 1,425 ATMs as of June 2024.

Key Financials Indicators

Particulars	FY24	FY23
Total assets (INR billion)	1,545.05	1,459.12
Total equity (INR billion)	121.92	98.96
Net income (INR billion)	17.67	11.97
Return on average assets (%)	1.2	0.9
Equity/assets (%)	7.9	6.8
Capital adequacy ratio (%)	15.3	15.4
Source: Company, Ind-Ra		

Correction in Previous Rating Action Commentary

Ind-Ra corrects the complexity indicator for basel III compliant Tier 2 bonds to Moderate from Low for the rating action commentary published on 23 August 2023.

Status of Non-Cooperation with previous rating agency

Not applicable

Rating History

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook			
	Rating Type	Rated Limits (billion)	Rating	23 August 2023	30 August 2022	24 February 2022	31 January 2022
Issuer rating	Long-term	-	IND AA-/Stable	IND A+/Positive	IND A+/Stable	IND A+/Stable	IND A+/Stable
Basel III Compliant Tier 2 bonds	Long-term	INR40	IND AA-/Stable	IND A+/Positive	IND A+/Stable	IND A+/Stable	IND A+/Stable

Complexity Level of the Instruments

Instrument Type	Complexity Indicator
Basel III compliant Tier 2 bonds	Moderate

For details on the complexity level of the instruments, please visit https://www.indiaratings.co.in/complexity-indicators.

Annexure

ISIN	Instrument	Date of Issue	Date of Issue	Maturity Date	Size of Issue (billion)	Rating/Outlook
INE168A08046	Basel III compliant Tier 2 bonds	28 December 2017	9.25	27 December 2024	INR5	IND AA-/Stable
INE168A08079	Basel III compliant Tier 2 bonds	30 March 2022	9.5	30 March 2032	INR3.6	IND AA-/Stable
	Total unutilised				INR31.4	
	Total				INR40	

Source: JK Bank, NSDL

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APPLICABLE CRITERIA

Rating Bank Subordinated and Hybrid Securities

Evaluating Corporate Governance

Financial Institutions Rating Criteria

The Rating Process