

India Ratings Revises Jammu and Kashmir Bank's Outlook to Positive; Affirms 'IND A+'

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India Ratings and Research (Ind-Ra) has revised Jammu and Kashmir Bank Limited's (JK Bank) Outlook to Positive from Stable while affirming the Long-term Issuer Rating at 'IND A+'. The instrument-wise rating action is as follows:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (billion)	Rating/Outlook	Rating Action
Basel III compliant Tier II bonds*	-	-	-	INR40	IND A+/Positive	Affirmed; Outlook revised to Positive from Stable

*Details in annexure

Analytical Approach: Ind-Ra continues to consider JK Bank's wholly-owned subsidiary, JKB Financial Services Ltd., in its analysis to arrive at the ratings.

JK Bank, on account of its unique and strategic place in the socially and politically-sensitive union territories of Jammu & Kashmir and Ladakh (UTJKL; formerly together the state of Jammu and Kashmir), has witnessed one geographical calamity, one large socio-political disturbance event, abrogation of article 370 and COVID-19-related disruptions over the past decade. The bank has received regulatory forbearances on account of these events.

The Outlook revision reflects the improvement in JK Bank's operating and financial metrics, asset quality and performance of standard restructured assets, and systems and processes in FY23. The Outlook also reflects the bank's infusion of external talent over the past two to three years to bring about best practices and lower need to provide for legacy stressed assets. While its capital buffers are lower than most banks', they have improved over the past two-three years and will continue the trend in view of its capital raising plans. In addition, the improving business socio-political environment in the two union territories that is aiding tourism, agriculture and small businesses adds to the bank's business proposition.

Key Rating Drivers

Improving Asset Quality: The bank's gross non-performing assets (GNPAs) improved to 6% at FYE23 (FYE22: 9.1%), supported by higher recoveries and higher upgrades of INR77 billion (INR27 billion). Furthermore, the slippages reduced to INR9.9 billion during 4QFY23 (3QFY23: INR24.84 billion), which led to better GNPA and net NPA ratios of 6.0% and 1.6%, respectively, than in FY22. Excluding the technical write-offs, the provision coverage stood robust at 74% in

4QFY23 (FY22: 73.2%). While the restructured standard portfolio also reduced to about INR12 billion in FY23 (FY22: INR15.52 billion), disproportionate slippages are likely from the restructured pool of assets. However, Jammu and Kashmir had seen increased number of tourists in FY23 and FY24, totalling 18.8 million in 2022 and about 18.9 million for January to July 2023 as against the yearly average of 2million -3million during pre-covid period. The bank believes this will play an important role in improving the performance of restructured assets. While fresh slippages, especially from the restructured and pandemic-affected pools, would weigh somewhat on the asset quality, the healthy provision on GNPA would help the bank manage slippages in FY24 and FY25.

Systemic Importance: 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 was present when the regions were administered by state of Jammu & Kashmir, the bank's capital levels were precariously close to the regulatory levels, given the loan concentration and the higher dependence on the government for timely and adequate infusion than most centre-owned mainstream scheduled commercial banks'. An improvement in UTJKL's socio-political situation over the medium to long term will aid JK Bank's capital levels.

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; the regions are governed by the central government since they are union territories.. The shareholding of the government of J&K and government of Ladakh also has declined to 63% from 70% as on March 2022 on account of the bank raising equity through Employee Stock Purchase Scheme. The bank has been re-designated as the agent bank by the Reserve Bank of India for UTJKL. It has also been re-designated as the governor's convenience bank for the JK Union Territory Level Banks Committee.

Liquidity Indicator - Adequate: JK Bank had no cumulative mismatches in the short-term bucket, with a funding surplus of around 12% of the total assets on asset-liability management in the up to one-year maturity bucket at FYE23. This is because it maintained about 20% of the total assets in government securities at FYE23. Moreover, it has a liquidity coverage ratio of 202.43% at FYE23, against the regulatory requirement of 100%.

Improved Profitability, Led by Low Credit Costs; though Cost Base Remains High : After having witnessed a loss of INR11.4 billion in FY20 with credit costs of 4.1%, JK Bank reported return on assets of 0.38%, 0.4% and 0.87%, respectively, during FY21, FY22 and FY23, due to a continued decline in the credit costs (0.1%; 0.4%, 1.6%). Moreover, the bank's profit increased to INR11.97 billion in FY23 (FY22: INR5.02 billion) and further INR3.5 billion in 1QFY24. Ind-Ra expects the bank's credit costs to remain low in FY24. Furthermore, the bank expects a major jump in its recoveries from the written-off assets in FY24 (FY23: INR2 billion; 1QFY24: INR1 billion). The bank's cost to income ratio, although improved, remained high at 66.2% in FY23 (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. Overall, Ind-Ra expects the profitability to sustain and further improve in the near to medium term.

Deposit Base Reasonable: At FYE23, the bank's current account saving account (CASA) ratio remained stable at 54.10% (FY22: 56.6%, FY21: 56.9%), with overall deposits rising 6.39% yoy, largely driven by growth in savings accounts due to its geographic presence in UTJKL. Its CASA ratio being better than that of most peers due to the majority government ownership, has helped the bank sustain traction in retail deposits over the years, as a major portion of the deposits belong to the JK region (FYE23: 87.42% of total deposits, FY22: 88.4%, FY21: 87.9%). The bank's term deposits grew 12.41% yoy to INR560.19 billion in FYE23. Overall, the bank's deposit profile plays an important role to maintain its margins (FY23: 4.2%; FY22:3.7%) . The cost of deposits, which stood at 3.79% at FYE23 (FY22: 3.65%, FYE21: 4.10%), is one of the lowest rates among Indian scheduled commercial banks, implying lower-than-peers' deposit costs.

Improvement in Operational Process Underway: The bank has appointed a new managing director and chief executive officer, Baldev Prakash, who has over three decades of experience in the banking industry outside the union territory of J&K. Hence, there has been an improvement in the processes through the setting up of regional processing centres for efficiency, and a consistency in approach towards credit, which should augur well on the asset side. The bank has also started bringing in outside talent in other top management levels as against earlier where hiring was exclusively for the

residents of erstwhile state of Jammu & Kashmir. Ind-Ra expects the new management to use their experience for better staff training, and streamlining process and controls. Ind-Ra expects these factors to play a positive role in improving the bank's systems and processes, resulting in higher credit originations, and improved monitoring, training and governance.

Improving but Still Low Capital Buffers; Further Improvement Expected: JK Bank's common equity tier 1 (CET1) stood improved to 11.05% in FY23 (FY22: 10.35%, FY21: 8.82%). Ind-Ra expects CET1 to improve to over 13% by FY24, supported by adequate profitability and plans of raising equity through a qualified institutional placement in 2HFY24. The bank in December 2022 raised INR10 billion as Tier-II bonds Ind-Ra also expects the bank to increase its capital buffers higher than those of peers, as it has to mitigate higher loan concentration and socio-political risks, while it also has a large retail segment in J&K that is supported by state and govt entities employees. The UTJKL government has infused equity in the bank in the past, when required, and the agency expects the support to continue.

Rating Sensitivities

Positive: The ability of the bank to increase the capital buffers as expected and maintain them sufficiently above the regulatory requirements on a sustained basis, reduce the geographical concentration in the J&K region, expand the margins, process improvement measures, maintain stable profitability from the core lending operations and no 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 raise larger questions on the propriety of the bank's processes
- larger-than-expected asset quality issues, leading to a decline in the CET 1 ratio below 10% on 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 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](#).

Company Profile

Srinagar-based JK Bank was established in 1938. It is majority-owned (63.41% as of March 2023) by the government of UTJKL. The bank had 985 branches and 1,425 ATMs as of March 2023.

FINANCIAL SUMMARY - CONSOLIDATED

Particulars	FY23	FY22
Total assets (INR billion)	1459.6	1,306.02
Total equity (INR billion)	99.43	81.07
Net income (INR billion)	11.97	5.02
Return on average assets (%)	0.9	0.4
Equity/assets (%)	6.8	6.2

Capital adequacy ratio (%)	15.4	13.23
Source: Company, Ind-Ra		

Non-Cooperation with previous rating agency

Not applicable

Solicitation Disclosures

Additional information is available at www.indiaratings.co.in. The ratings above were solicited by, or on behalf of, the issuer, and therefore, India Ratings has been compensated for the provision of the ratings.

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Rating History

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



Annexure

ISIN	Instrument	Date of Issue	Coupon Rate (%)	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 A+/Positive
INE168A08079	Basel III compliant Tier 2 bonds	30 March 2022	9.50	30 March 2032	INR3.6	IND A+/Positive
	Total unutilised				INR31.4	
	Total				INR40	

Bank wise Facilities Details

[Click here to see the details](#)

Complexity Level of Instruments

Instrument Type	Complexity Indicator
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For details on the complexity level of the instruments, please visit <https://www.indiaratings.co.in/complexity-indicators>.

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APPLICABLE CRITERIA

Rating Bank Subordinated and Hybrid Securities

Financial Institutions Rating Criteria

Evaluating Corporate Governance

The Rating Process

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