

Press Release
The Jammu And Kashmir Bank Limited

March 03, 2020

Rating Assigned



Total facilities	Rs. 1600.00 Cr.
Total BASEL III Compliant Tier-2 Bonds	Rs. 1050.00 Cr.
Long Term Rating	ACUITE AA- /Stable (Assigned)
Total BASEL III Compliant Additional Tier-1 Bonds	Rs.550.00 Cr.
Long Term Rating	ACUITE A+ /Stable (Assigned)

* Refer Annexure for details

Rating Rationale

Acuité has assigned the long-term rating of '**ACUITE AA-**' (read as **ACUITE double A minus**) on the Rs.1050.00 Cr. Non-Convertible Basel III Compliant Tier-2 Bonds of The Jammu & Kashmir Bank Limited (JKB). The outlook is '**Stable**'.

Further, Acuité has assigned the long-term rating of '**ACUITE A+**' (read as **ACUITE A plus**) on the Rs.550.00 Cr. Basel III Compliant Additional Tier-1 Bonds of The Jammu & Kashmir Bank Limited (JKB). The outlook is '**Stable**'.

About the bank:

Established in 1938, The Jammu & Kashmir Bank Limited (J&K Bank) is a scheduled commercial bank. J&K Bank is a private sector bank with Government of Jammu & Kashmir* as a promoter holding 59.23% stake in the bank as on December 31, 2019. JKB has a branch network of 955 branches (825 in region of Jammu and Kashmir and Ladakh and remaining spread across rest of India (ROI)). The bank has been listed on BSE and NSE since 1998.

Analytical Approach

Acuité has adopted a consolidated approach while assessing the business and financial risk profiles of JKB along with its subsidiary JKB Financial Services Ltd. Additionally, the majority Government ownership and the ongoing support from the Government of Jammu & Kashmir has been factored in the rating. Acuité has maintained a differential rating of one notch between the Proposed Non-Convertible Basel III Compliant Tier 2 Bond and Proposed Non-Convertible Basel III Compliant Tier 1 bonds. The differential in rating is due to the higher loss absorption characteristics associated with the Tier-1 bond.

Key Rating Drivers

Strengths

- **Pivotal position in the Jammu & Kashmir region:**

The Jammu & Kashmir Bank (JKB) was established in 1938. With a track record of over eight decades it holds a key position in the UT of Jammu & Kashmir. As per RBI data, Jammu & Kashmir (J&K) region's deposits were Rs.1.18 lakh Crore as on March 31, 2019. JKB's deposit base as on March 31, 2019 was Rs. 78,759 Crore indicating a 67% share in the overall deposits from the region. Similarly, JKB accounted for 69% of the overall credit in the region. JKB is also the preferred banker for all the J&K State Government enterprises and employees. Being the largest bank in the UT it forms an integral part of the UT's economic nervous system. JKB has a branch network of 825 branches (in UT of J&K and Ladakh) being the largest spread branch network within the region. RBI has appointed JKB as the lead convenor bank for the UT of Jammu & Kashmir.

Foot notes:

*the Government of India has passed the Jammu & Kashmir reorganization Act recently under which the erstwhile state of Jammu & Kashmir has been reorganized into UT of Jammu & Kashmir and UT of Ladakh w.e.f. from October 31, 2019. Both these UT's will be governed by their respective Lieutenant Governor.

JKB is a scheduled commercial bank, with 59.23% stake held by the government of J&K and Ladakh. The bank continues to receive support from the Govt. of Jammu & Kashmir whether in the form of growth or distress funding on an ongoing basis. In FY2020 the bank expects ~Rs.500 Cr. equity infusion from the Govt. of Jammu & Kashmir which is expected to increase its stake to 68% (approximate figure). This infusion is expected to partly offset the losses of the bank during FY2020.

Given its status as a dominant commercial bank in J&K, JKB is expected to play a key role in the economic development of the region and also act as an implementation vehicle for the various government schemes. Considering the socio-political sensitivity of the region and the pivotal position of the bank in that region, Acuite believes that JKB will be strategically important for the Government and it will continue to support the bank through regular financial and managerial support.

- **Healthy base of low cost deposits**

Based on its extensive branch network in the J&K region the bank has been able to mobilise deposits from a large retail base which forms ~93% of its funding profile. The bank maintained a healthy current accounts savings accounts ratio of 51.54% as on December 31, 2019 and 50.7% as on March 31, 2019 which compares favorably with the CASA ratios of some other leading banks like SBI (@ 44.2%), HDFC Bank (@41.4%), BOB (@35.0%). Besides deposits from general public the bank is also the preferred banker for J&K State run enterprises and employees. ~21% of JKB's deposits come from J&K Government run enterprises and employees.

The continued access to low cost deposits has resulted in robust Net Interest Margins (NIM) for JKB ranging between 3.7% – 4.3% over the past three years.

Acuite believes that the steady flow of retail deposits and the established retail franchise augurs well for the future profitability of the bank.

Weaknesses

- **Susceptibility to socio-political climate in the Jammu & Kashmir region**

The state of Jammu & Kashmir was formed in 1948, and was accorded special status under Article 370 in 1954. The region Jammu & Kashmir since then has been subject to two major wars and various socio-political hindrances, which has frequently hampered the livelihood and thus economy of the region. Recently, Union of India revoked the special status of Article 370 accorded to the then state of Jammu and Kashmir and reorganized it into UT of Jammu & Kashmir and Ladakh. The bank still relies on the J&K region for major part of its business (90% of deposits, 62% of advances and 86% of branches).

Acuite believes, that in view of the recent political developments, the trade and commerce activities in the region could be impacted over the near term. Any action initiated by the Government to maintain law and order level such as discontinuance of internet and other services will have an impact on the level of activity in the region, especially in case of those activities which has a high reliance on these services. The region has always been a subject of dispute with other countries and hence has always exhibited high degree of social and political volatility. Any continuation of high social instability is likely to result in lower levels of activity in respect of sectors like tourism which are the major thrust areas for the government.

Acuite believes that, the banks growth trajectory and future operating performance will depend upon the continued government focus on providing a healthy operating environment in the J&K region, thereby paving the way for attracting fresh investment and sustainability of existing business.

- **Build-up of asset quality pressures and its impact on capital position**

The asset profile of the bank can be classified into a two distinct segments, the retail loan book is mainly located within the UT of Jammu & Kashmir and Ladakh while the corporate loan book mainly lies in the Rest of India (ROI). Agriculture and tourism being the major economic drivers of the UT, is impacted by natural calamities (floods in 2016) and unrest due to socio-political developments. This has resulted in delinquencies and restructuring of loans in the past. The disruption in activities in the Kashmir Valley post changes in political dispensation, resulted in unrest and consequently increase in delinquencies in JKB's retail portfolio. As on December 31, 2019 the gross non-performing assets (GNPA) from the retail portfolio increased to 3.0% of overall retail portfolio from 1.2% as on March 31, 2019.

39% of JKB's book is from corporate advances, this portfolio has witnessed major increase in delinquencies over the past few fiscals. Corporate book GNPA rose from 16.6% of the corporate book as on March 31, 2019 to 20.4% as on December 31, 2019. Overall GNPA stood at 11.1% as on December 31, 2019 as against 8.97% as on March 31, 2019. The bank however, maintained a provisioning coverage of 73% as on December 31, 2019.

Off the overall GNPA's 54% were from the Top 20 NPA accounts, out of these 25% of the top 20 NPA was from

single borrower group with an outstanding balance of Rs. 1043 Cr. As per Acuite discussions with the bank, the bank plans to decrease its large ticket exposure (i.e. exposures above Rs. 200-300 Cr. in order to avoid impact of delinquency in such wholesale exposures).

The increase in delinquencies has also resulted in higher credit costs resulting in moderation in profitability and increase in losses. Loss for 9 months ending December 31, 2019 stood at Rs. 845 Cr. While the bank has maintained a higher than required Capital adequacy ratio (CRAR), Common Equity Tier(CET)-1 CRAR has declined significantly from 9.13% as on March 31, 2019 to 8.15% as on December 31, 2019. The total CRAR is expected to be between 12.0% -12.9% for FY2020. The improvement is expected to be backed by support in the form of equity infusion of Rs. 500 Cr. by the Govt. of Jammu & Kashmir and Tier 2 issuance of Rs. 1050 Cr. in the last quarter of the current fiscal.

Acuite believes that lowering of credit costs (due to lower slippages) and consequent improvement in profitability will be key monitorables.

Rating Sensitivity

Negative

- Reduction in capital adequacy buffers to below 0.5% over threshold levels;
- Increase in asset quality pressures and continued losses;
- Outcome of ongoing investigations likely to impact the performance;

Positive

- Significant improvement in asset quality;
- High level of geographic diversification while maintaining/Improving asset quality and profitability parameters;
- Definite documented confirmation from the Government regarding willingness to support the bank for its growth/distress capital needs.

Liquidity Position: Strong

JKB's asset-liability tenure is well matched with no cumulative negative mismatches up to the one-year bucket. The bank had a high current account savings account ratio of 51.5% for 9MFY2020 (FY19: 50.7%), The bank's liquidity coverage ratio was about 262.2% at 9MFY2020 against the regulatory requirement of 100% as on December 31, 2019.

Outlook: Stable

Acuite believes that JKB will maintain a 'Stable' outlook on the back of continuing support from Government of Jammu & Kashmir and its pivotal position in the region of Jammu and Kashmir. The outlook may be revised to 'Positive' in case JKB is able to demonstrate a significant and sustainable improvement in asset quality, profitability and capital adequacy parameters coupled with stated intent of the Government to support the bank. The outlook may be revised to 'Negative' in case the bank faces challenges in attaining a significant improvement in asset quality, profitability and capital adequacy parameters or in case of extremely adverse outcomes from the ongoing investigations by regulatory authorities.

About the Rated Entity - Key Financials

Parameters	Unit	FY19 (Actual)	FY18 (Actual)	FY17 (Actual)
Interest Income	Rs. Cr.	7676	6621	6684
Interest Expense	Rs. Cr.	4292	3751	4174
Profit After Tax (PAT)	Rs. Cr.	465	203	(1632)
Deposits	Rs. Cr.	89639	80006	72463
Net Advances	Rs. Cr.	66272	56913	49816
Investments	Rs. Cr.	23161	18880	21291
Capital Adequacy	(%)	12.46	11.42	10.80
Return on Average Assets (RoAA)	(%)	0.49	0.24	(2.01)
Gross NPA	(%)	8.97	9.96	11.20
Net NPA	(%)	4.89	4.90	4.87

Status of non-cooperation with previous CRA (if applicable)

None

Any other information

None

Material Covenants

None

Applicable Criteria

- Banks and Financial Institutions: <https://www.acuite.in/view-rating-criteria-45.htm>
- Financial ratios and Adjustments: <https://www.acuite.in/view-rating-criteria-20.htm>
- Default Recognition: <https://www.acuite.in/view-rating-criteria-17.htm>

Note on complexity levels of the rated instrument

<https://www.acuite.in/criteria-complexity-levels.htm>

Rating History (Upto last three years)

Not Applicable

***Annexure – Details of instruments rated**

ISIN	Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
-	Proposed Basel III Compliant Tier-2 Bonds	-	-	-	1050.00	ACUITE AA-/Stable (Assigned)
-	Proposed Basel III Compliant Additional Tier-1 Bonds	-	-	-	550.00	ACUITE A+/Stable (Assigned)

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About Acuité Ratings & Research:

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