Jammu & Kashmir Bank Limited

September 20, 2022

Rating

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Tier-II bonds (Basel-III)-I[#]	1,000.00	CARE A+; Stable (Single A Plus; Outlook: Stable)	Reaffirmed
Total long-term instruments	**1,000.00 (₹ One thousand crore only)**		

Details of instruments/facilities in Annexure-1.

[#]Tier-II bonds under Basel-III are characterised by a 'point of non-viability' (PONV) trigger due to which the investor may suffer a loss of principal. The PONV will be determined by the Reserve Bank of India (RBI) and is a point at which the bank may no longer remain a going concern on its own unless appropriate measures are taken to revive its operations, and thus, enable it to continue as a going concern. In addition, the difficulties faced by a bank should be such that these are likely to result in financial losses and raising the common equity Tier-I (CET-I) capital of the bank should be considered as the most appropriate way to prevent the bank from turning non-viable. In CARE Ratings Limited's (CARE Ratings') opinion, the parameters considered to assess whether a bank will reach the PONV are similar to the parameters considered to assess the rating of the Tier-II instruments even under Basel-II. CARE Ratings has rated the Tier-II bonds under Basel-III after factoring in the additional feature of the PONV.

Detailed rationale and key rating drivers

The rating assigned to the debt instrument of Jammu & Kashmir Bank Limited (JKB) factors in the majority ownership by the Government of the Union Territories of Jammu & Kashmir and Ladakh (UTJKL) (68% of the shareholding as on June 30, 2022), JKB's long track record of operations with a dominant position in the UTJKL, and its strong resource profile characterised by the relatively higher proportion of current account savings account (CASA) deposits. The rating takes note of the slight improvement in the capital adequacy levels, on account of the capital raised of ₹744 crore in FY22 (refers to the period from April 01 to March 31) and internal accruals. The capital adequacy ratio (CAR) and Tier-I CAR stood at 13.23% and 11.73%, respectively, as on March 31, 2022, as against 12.20% and 10.28%, respectively, as on March 31, 2021. However, the timely infusion of capital is critical to support the growth.

The rating is, however, constrained by the limited geographical diversification with moderate size of operations, moderate earnings profile, and moderate asset quality parameters.

Rating sensitivities

Positive factors – Factors that could lead to positive rating action/upgrade:

- Improved profitability on a sustained basis.
- Significant improvement in the capital adequacy from the present levels.

Negative factors – Factors that could lead to negative rating action/downgrade:

- Change in the support from the Government of the UTJKL.
- Deterioration in the asset quality profile.
- Deterioration in the capital, with Tier-I CAR below 10.5%.

Detailed description of the key rating drivers

Key rating strengths

Long track record of operations with the majority ownership by the UT of Jammu and Kashmir: JKB is a mid-sized, private sector scheduled commercial bank, with the UTJKL holding 68% of the stake as on June 30, 2022. The bank has a long and established track record of more than 80 years. It is the only private sector bank that has been designated as the RBI's agent for the banking business for the Government of UTJKL.
JKB holds a dominant position in the UTJKL with a significant market share in terms of business. Given the systemic importance of the bank to the economy of the UTJKL, the government has demonstrated continuous need-based support to the bank, which has helped the bank maintain adequate CAR levels.

Dominant presence in the UTJKL: JKB is the leading bank in the UTJKL and is designated as an agency bank by the RBI for carrying out the banking business for the Government of Jammu & Kashmir and Ladakh. The bank holds a dominant position in the region with a significant market share in terms of advances and deposits. Of the total number of branches, ie, 980 as on March 31, 2022, 817 branches are in the UTJKL.

Strong deposit base with a relatively high proportion of CASA: Owing to JKB's strong market position in the Union Territory of Jammu & Kashmir and the Union Territory of Ladakh, its deposit mobilisation capability within the state remains strong. The bank has a strong resource profile, as depicted by the significant proportion of low-cost steady CASA deposits,

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

which remained at 57% as on March 31, 2022, and 56% as on June 30, 2022 (PY: 57% as on March 31, 2021). Notably, in the last five years, the CASA proportion stood in the range of 52% to 57%. CARE Ratings expects the proportion of the CASA to remain at similar levels over the medium term, with the bank having a dominant position in UTJKL.
The total deposits increased by 6% to ₹114,710 crore as on March 31, 2022 (June 30, 2022: ₹112,145 crore) as against ₹108,061 crore as on March 31, 2021. The proportion of retail deposits (as a percentage of term deposits) stood at 75% as on March 31, 2022, as against 80% as on March 31, 2021.

Improvement in capital adequacy levels: As on March 31, 2022, the bank reported a total CAR of 13.23%, Tier-I CAR of 11.73%, and CET-I of 10.35%, as against 12.20%, 10.28%, and 8.82%, respectively, as on March 31, 2021. In FY22, the bank raised capital of ₹744 crore, of which ₹500 crore was received from the Government of the UT of Jammu & Kashmir, ₹150 crore by way of the Employee Stock Purchase Scheme, and ₹94 crore via qualified institutional placement (QIP). In addition to this, the bank also raised Tier-II bonds aggregating to ₹360 crore during Q4FY22. The total CAR stood at 13.02%, with Tier-I CAR and CET-I at 11.55% and 10.19%, respectively, as on June 30, 2022, against the regulatory minimum requirements (including capital conservation buffer [CCB]) of 11.50%, 9.50%, and 8.00%, respectively. The bank has received continuous support in terms of capital from the government, however, the bank's ability to raise capital in a timely manner to maintain the capitalisation profile will be critical for its credit profile and growth.

Key rating weaknesses

Moderate asset quality: The bank has faced challenges with asset quality in the past; however, with write-offs and recovery efforts, the asset quality of the bank has improved. Despite an improvement in the asset quality indicators during FY22, it continues to be moderate, with the gross non-performing assets (GNPA) and net non-performing assets (NNPA) at 8.67% and 2.49%, respectively, as on March 31, 2022, as against 9.67% and 2.95%, respectively, as on March 31, 2021. The improvement in the GNPA levels during the year can be attributed to better recoveries and upgrades. The GNPA and NNPA stood at 9.09% and 3.02%, respectively, as on June 30, 2022.
The bank has restructured advances aggregating to ₹3,208 crore, of which around 36% of the restructured portfolio is on account of the COVID-19 Resolution Framework 1 & 2, and the remaining restructured portfolio is due to the flood and political unrest at different times in the past. The total gross stressed assets (standard restructured asset + security receipts outstanding + GNPA) of the bank stood at 10.84% as on March 31, 2022, as against 10.66% as on March 31, 2021 (11.10% as on June 30, 2022). The bank has also disbursed the emergency credit line guarantee scheme (ECLGS) aggregating to ₹1,928 crore (2.56% of the portfolio). Of the total restructured portfolio of ₹1,147 crore as on June 30, 2022, under the COVID-19 Resolution Framework 1 & 2, ₹134 crore has already slipped into non-performing assets (NPAs).

Moderate earnings profile with high cost to income: The bank reported a profit-after-tax (PAT) of ₹502 crore in FY22 against ₹432 crore in FY21. The net interest margin (NIM) declined to 3.15% in FY22 from 3.33% in FY21. The non-interest income as a percentage of the total assets was maintained at 0.63% in FY22. However, the cost to income continues to remain relatively high, at 76% in FY22 as against 64% in FY21. The increase in the operating expenses is mainly on account of an increase in the one-time expense of ₹319 crore due to the medical allowance and adjustment pay components of the pension fund recorded in FY22. The bank reported a pre-provisioning operating profit (PPOP) of ₹1,099 crore in FY22 as against ₹1,611 crore in FY21. With a reduction in the credit cost during the year, the bank reported a return on total assets (ROTA) of 0.40% in FY22 (PY: 0.38%).
During Q1FY23, the bank reported a PAT of ₹166 crore as against ₹104 crore during Q1FY22. The bank continues to incur high operating expenses in Q1FY23 with cost to income at 69% on account of the high employee cost. With a reduction in the credit cost, the bank has reported a ROTA of 0.52% in Q1FY23 as compared with 0.35% in Q1FY22.

Limited geographical diversification with moderate scale of operations: With total gross advances of ₹75,242 crore and deposits of ₹114,710 crore as on March 31, 2022, JKB is a mid-sized bank as compared with other public and private sector peers. The bank's operations are regionally concentrated, with 88% of the bank's deposits and 73% of its advances emanating from J&K as on March 31, 2022. Owing to the bank's high reliance on J&K, any political unrest or administrative and business instability in the region is likely to impact the bank's growth, asset quality, and profitability.
JKB's gross advances grew by 5% in FY22 and stood at ₹75,242 crore as on March 31, 2022 (PY: ₹71,917 crore) and deposits grew by 6% and stood at ₹114,710 crore as on March 31, 2022 (PY: ₹108,061 crore).

Liquidity position: Adequate

As per the structural liquidity statement of the bank, as on June 30, 2022, the bank has no negative cumulative mismatches across all its time buckets up to one to three years. The bank had excess statutory liquidity ratio (SLR) holdings of ₹9,725 crore as on June 30, 2022. The liquidity coverage ratio (LCR) as on June 30, 2022, stood at 171% against the minimum regulatory requirement of 100%

Analytical approach: Standalone

Applicable criteria
Criteria on assigning 'outlook' and 'credit watch' to credit ratings
CARE Ratings' policy on Default Recognition
Financial ratios – Financial sector
CARE Ratings' rating methodology for banks
Rating Basel-III – Hybrid capital instruments issued by banks

About the bank
JKB, a private sector scheduled commercial bank, was incorporated on October 1, 1938, and commenced business from July 4, 1939, from Srinagar, Kashmir. The bank functions as a leading bank in the UTJKL and is designated by the RBI as its exclusive agent for carrying out the banking business for the Government of J&K and Ladakh. JKB is the only state government (now Government of UT)-owned bank in the country, and the Government of the UT of J&K (GoJK) holds around 68% stake in the bank as on June 30, 2022. JKB holds a dominant position in the UT of J&K, constituting majority of the credit and deposits in the state. As on June 30, 2022, it operated through a network of 980 branches and 1,410 ATMs. While predominantly focused in J&K, the bank has spread over 18 states and four UTs. The bank remains largely rural focused, with 55% of the total branches (as on March 31, 2022) in rural areas, followed by 18% in metro, 17% in semi-urban, and the remaining 11% in urban locations.

Brief Financials (₹ crore)	FY21(A)	FY22(A)	Q1FY23(P)
TOI	8,830	8,794	2,306
PAT	432	502	166
Interest coverage (times)	1.37	1.27	1.36
Total assets	1,19,054	1,29,413	1,28,376
Net NPA (%)	2.95	2.49	3.02
ROTA (%)	0.38	0.40	0.52

A: Audited; P: Provisional.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of the various instruments rated for this company: Annexure-4

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Tier-II bonds (Basel-III)-I	INE168A08079	March 30, 2022	9.50%	March 30, 2032	360.00	CARE A+; Stable
Proposed Tier-II bonds (Basel-III)-I	-	-	-	Proposed	640.00	CARE A+; Stable

Annexure-2: Rating history for the 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 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1.	Bonds-Lower Tier-II	LT	-	-	-	-	-	1)Withdrawn (March 13, 2020) 2)CARE AA- (CWN) (October 03, 2019) 3)CARE AA- (CWN) (August 13, 2019)
2.	Bonds-Tier-II bonds	LT	1,000.00	CARE A+; Stable	-	1)CARE A+; Stable (March 09, 2022)	-	-

*Long term/short term.

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities

Name of the Instrument	Detailed Explanation
Non-financial covenants	
Conditions for exercise of call option for Tier-II bonds (Basel-III)-I	The bank has call option on or after the fifth anniversary from the date of issue, subject to prior supervisory approval.

Annexure-4: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity level
1.	Bonds-Tier-II bonds	Complex

Annexure-5: Bank lender details for this company

To view the lender-wise details of the bank facilities, please click here.

Note on complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.infor any clarifications.

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About us:
Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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