March 21, 2024

Jharkhand Rajya Gramin Bank: Rating reaffirmed; Outlook revised to Positive

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Perpetual debt programme (Tier I bonds)	300.00	300.00	[ICRA]BBB+ (Positive); reaffirmed and outlook revised to Positive from Stable
Total	**300.00**	**300.00**	

**Instrument details are provided in Annexure I*

Rationale

The revision in the outlook on the long-term rating of Jharkhand Rajya Gramin Bank (JRGB) factors in the improvement in its capital profile and profitability metrics. Moreover, as the pension liabilities are expected to be largely provided for in FY2024, the bank's internal capital generation is expected to improve further, leading to an improvement in its ability to grow the loan book as well as solvency profile[1].

ICRA notes that the bank's operations remain focused on rural credit in Jharkhand, limiting its overall scale and growth prospects while keeping the geographical and sectoral concentration of the loan book high. The significant contribution of crop and agricultural loans to total gross advances also poses asset quality risk due to agro-climatic conditions as well as the political appeasement of farmers via farm loan waiver announcements, especially during election years. Additionally, although the headline asset quality indicators have improved due to the lag in the recognition of non-performing advances (NPAs) for agricultural loans over two crop cycles as well as the high level of overdue loans (special mention account (SMA) 0, 1 and 2), JRGB's ability to keep its slippages under control and reduce its overdue loan book will remain monitorable from the asset quality as well as profitability perspective.

The rating continues to consider the bank's parentage, with the Government of India (GoI) holding a 50% stake, the Government of Jharkhand (GoJ) holding 15% and State Bank of India {SBI; rated [ICRA]AAA (Stable) for Tier II bonds} holding 35%. Further, JRGB is incorporated under the Regional Rural Banks Act, 1976, under which the combined holding of the GoI and the sponsor bank (SBI) is to be maintained at 51%, thereby ensuring sizeable direct or indirect sovereign ownership at all times. Moreover, regional rural banks (RRBs) remain strategically important to the GoI and state governments for meeting the credit demands of the agriculture sector.

The rating also factors in JRGB's deposit profile, which remains highly granular, given its rural presence as well as the high share of current account and savings account (CASA) in total deposits, translating into a competitive cost of funds. Hence, despite the lower credit-to-deposit (CD) ratio, JRGB's profitability is supported by its competitive cost of funds. Moreover, given the sizeable holding of Government securities, its overall profitability remains dependent on mark-to-market gains/losses in the bond portfolio.

The Positive outlook on the rating factors in ICRA's assessment that the bank will continue to maintain the improvement in its asset quality and earnings profile and is better placed to grow as well as absorb asset quality shocks while keeping the capital ratios above the regulatory levels.

[1] Solvency is defined as (Net NPA + Unprovided pension liability)/Core equity capital

Key rating drivers and their description

Credit strengths

Strong parentage and constitution under RRB Act – JRGB is incorporated under the Regional Rural Banks Act, 1976 and is jointly owned by the GoI, the GoJ and SBI. Legislative amendments introduced to the RRB Act in 2015 prevent the dilution of the combined holding of the GoI and the sponsor bank below 51%, thereby ensuring sizeable direct or indirect sovereign ownership in JRGB. Furthermore, under the Act, the GoI appoints the Chairman and two directors on the board, while the state government is represented by two nominee directors. SBI, on the other hand, is represented by two directors nominated by it. Additionally, the board has representatives from National Bank for Agriculture and Rural Development (NABARD) and the Reserve Bank of India (RBI).

SBI and NABARD closely monitor the operational and financial performance of RRBs and extend supervisory support on a periodic basis. However, ICRA notes that while SBI remains the sponsor bank for JRGB, any change in the sponsor bank, under a scheme of amalgamation of RRBs, will remain monitorable. Further, given the requirement of maintaining the requisite shareholding pattern, capital infusions must be supported by all the shareholders.

Deposit profile characterised by high share of CASA and granularity – JRGB had 445 branches as on December 31, 2023 spread across the rural and semi-urban regions of Jharkhand. The rating also factors in the bank's deposit profile, which remains inherently granular, given its presence in rural areas, as well as the high share of CASA, which stood at ~67% as on February 29, 2024 and 68% as on March 31, 2023 (RRB average of ~55% as on March 31, 2023). The steady and strong CASA base, coupled with the granular term deposit base, has helped the bank maintain a competitive cost of interest-bearing funds (4.07% in 11M FY2024). Moreover, the cost of interest-bearing funds of 3.92% in FY2023 was lower than the RRB average of 4.02% in FY2023. However, this was also driven by the steady CASA deposit growth and the limited need to mobilise term deposits, given JRGB's low CD ratio. As internal accruals improve and with increasing focus on credit growth, incremental deposit mobilisation through term deposits will reduce the share of CASA deposits and push up the cost of funds.

Outlook on profitability improves – With the improvement in the yield on assets and the competitive cost of funds, the net interest margin (NIM) increased to 3.99% (annualised) of average total assets (ATA) in 11M FY2024 from 3.61% in FY2023, resulting in higher operating profitability of 2.81% (annualised) of ATA in 11M FY2024 vis-à-vis 2.74% in FY2023. As the pension liabilities are largely provided for and given the reduction in the credit costs due to the steady asset quality, the bank reported an improvement in its return on assets (RoA) to 1.48% (annualised) in 11M FY2024 from 0.76% in FY2023. Going forward, in the absence of any one-off events, JRGB is expected to maintain/further improve its net profitability metrics, although this will be subject to the asset quality performance.

Credit challenges

Asset quality remains a monitorable – JRGB witnessed an improvement in its headline asset quality indicators with the gross NPA (GNPA) and net NPA (NNPA) declining to 3.86% and 0.99%, respectively, as on February 29, 2024 from 4.80% and 1.19%, respectively, as on March 31, 2023. However, the overdue loan book (SMA 1 and 2) remained high in relation to the capital. Slippages from this pool could remain elevated in the near term, leading to higher credit costs and lower profitability. Further, there could be a lag in the recognition of stressed accounts as NPA for agricultural loans over two crop cycles, which may result in sudden asset quality pressure, given the high share of agricultural advances in the overall loan portfolio.

However, as the bank was able to provide for a major part of the pension liabilities, ICRA expects it to be in a better position to absorb credit losses in case of the weak performance of the overdue loan book in FY2025.

Growth in advances remains constrained, given limited capital buffers – JRGB's capitalisation profile appears to be comfortable with a CET I and CRAR of 11.2% and 12.5%, respectively, as on February 29, 2024 against the regulatory requirement of 9%[2]. This was on account of the lower risk-weighted assets (RWA) density because of the lower CD ratio (~58%

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[2] *RRBs need to maintain a minimum Tier I capital of 7.0%, and within the overall Tier I capital, perpetual debt instruments (PDIs) are restricted to 1.5%. In case the bank meets the CET of 5.5% and the Tier I of 7.0% with PDIs, the additional PDI over 1.5% is eligible for the calculation of the overall CRAR. Further, RRBs are not allowed to issue Tier II instruments and the current Tier II capital consists of standard assets*

as on February 29, 2024 against the RRB average of 68% as on March 31, 2023), leading to a high share of risk-free Government securities and bank deposits in the overall assets. Further, JRGB's CRAR of 11.31% as on March 31, 2023 was lower than the RRB average of 13.4%. Though the bank's pension liability increased to Rs. 734 crore from Rs. 694 crore due to wage revisions, only ~Rs. 15 crore remains to be provided for as on February 29, 2024. As a result, the solvency stood at 10% as on February 29, 2024 (19% as on December 31, 2022[3], 50% as on March 31, 2022). As pension liabilities will get largely provided for in FY2024, JRGB's internal capital generation is likely to improve from the current level, which will also support its growth and overall capitalisation profile.

Given the geographical limitations, the overall growth is likely to remain range-bound and growth-led capital consumption could be lower than capital accretion. The cushion above the regulatory levels could build up gradually, although this would remain contingent on the asset quality.

High geographical concentration and vulnerability to agro-climatic risks – RRBs were set up with the primary focus of meeting the credit demand of the agriculture sector, with a district-defined role for each RRB. As RRBs operate within a limited number of districts or a single state, the overall scale and growth prospects remain limited, resulting in the high geographical concentration of the loan book. JRGB's loan book is concentrated towards agricultural advances (constituting ~71% of gross advances as on September 30, 2023). High exposure to the agriculture sector, coupled with the marginal profile of the borrowers, exposes JRGB to agro-climatic risks, which could severely impact collections and lead to the deterioration of its asset quality metrics. Asset quality risk also arises from the political appeasement of farmers via farm loan waiver announcements, especially during election years. Further, the NPA recognition of agricultural loans is based on crop cycles (single or two crops in a year), which can result in delays in stress recognition. The bank saw a significant build-up in overdue loans in its agricultural loan book in H1 FY2024 and its ability to arrest slippages will be critical for its asset quality and profitability, going forward.

Liquidity position: Strong

The strong liquidity profile is driven by the statutory liquidity ratio (SLR) maintained by the bank, which was as high as 47% of the net demand and time liabilities (NDTL) as on September 30, 2023 because of the lower CD ratio against the regulatory requirement of 18%. JRGB has a high share of CASA deposits, which has helped it maintain positive cumulative mismatches in the less than one month maturity bucket as on September 30, 2023.

Rating sensitivities

Positive factors – ICRA could upgrade the rating if the bank is able to maintain its profitability metrics with an RoA of more than 1.2% while keeping the capital cushions more than 3% above the regulatory levels on a sustained basis. An improvement in the scale of operations and business risk profile will also be a positive factor.

Negative factors – Deterioration in the asset quality, leading to the weakening in the profitability, with RoA of less than 0.5%, or weakening of the capital cushions to less than 1% at the CET I, Tier I or CRAR level on a sustained basis could exert pressure on the rating.

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provisioning. Accordingly, even in a scenario where an RRB is able to raise sizeable PDIs, its ability to meet the overall CRAR will continue to be driven by its ability to meet the minimum CET of 5.5%

[3] *Based on previous estimate of pension liability of Rs. 694 crore*

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA's Rating Methodology for Banks and Financial Institutions Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group support	JRGB was incorporated under the Regional Rural Banks Act, 1976 and is jointly owned by the GoI, the GoJ and SBI. The RRBs remain strategically important to the GoI and state governments, with sizeable direct or indirect sovereign ownership. ICRA expects JRGB to receive financial support from its co-owners, if required.
Consolidation/Standalone	To arrive at the rating, ICRA has considered the standalone financials of JRGB. JRGB does not have any subsidiaries.

About the company

Jharkhand Rajya Gramin Bank (JRGB) was established on April 01, 2019 when the erstwhile Jharkhand Gramin Bank (sponsored by Bank of India) and Vananchal Gramin Bank (sponsored by SBI) were amalgamated into one entity. SBI (rated [ICRA]AAA (Stable) for Tier II bonds) is the sponsor bank of JRGB with a 35% stake. JRGB's head office is in Ranchi and its area of operations is the combined area of operations of the two erstwhile constituent banks. It has a network of 445 branches and 8 regional offices across Jharkhand.

JRGB reported a profit after tax (PAT) of Rs. 181 crore in 11M FY2024 (PAT of Rs. 94 crore in FY2023) on a total asset base of Rs. 13,935 crore as on February 29, 2024 (Rs. 12,766 crore as on March 31, 2023), translating into an RoA of 1.48% and 0.76%, respectively.

Key financial indicators

Jharkhand Rajya Gramin Bank	FY2022	FY2023	11M FY2024*
Total income^	493	577	568
Profit after tax	73	94	181
Total assets	11,976	12,766	13,935
CET I	10.02%	9.77%	11.19%
CRAR	11.71%	11.31%	12.45%
PAT/ATA	0.65%	0.76%	1.48%
Gross NPA	6.42%	4.80%	3.86%
Net NPA	1.98%	1.19%	0.99%

*Note: Amount in Rs. crore; Source: JRGB, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations*
^Total income = Net interest income + Non-interest income

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					March 21, 2024	March 14, 2023	March 16, 2022	March 22, 2021
1	**Perpetual debt – Tier I bonds**	Long term	300	Yet to be issued	[ICRA]BBB+ (Positive)	[ICRA]BBB+ (Stable)	[ICRA]BBB (Positive)	[ICRA]BBB(hyb) (Stable)

In compliance with the circular issued by the Securities and Exchange Board of India (SEBI) on July 16, 2021 for standardising the rating scales used by credit rating agencies, ICRA has discontinued its practice of affixing the (hyb) suffix alongside the rating symbols for hybrid instruments

Complexity level of the rated instrument

Instrument	Complexity Indicator
Perpetual debt programme (Tier I bonds)	Moderately Complex

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I : Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
-	**Perpetual debt – Tier I bonds**	Yet to be issued	-	-	300.00	[ICRA]BBB + (Positive)

Source: JRGB

Key features of the instrument

The rated Tier I bonds have specific features, whereby the debt servicing is linked to the bank meeting the regulatory norms for capitalisation and reported profitability. As per the regulatory norms for these debt capital instruments, approval from the RBI is required for debt servicing (including principal repayments) in case the bank reports a loss and it is not liable to service the debt if it breaches the minimum regulatory capitalisation norms, i.e. CRAR of 9.0%. The coupon, if not paid, is non-cumulative.

Annexure II: List of entities considered for consolidated analysis – Not applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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