CLSA India Forum

J&K Bank: Creatively Conservative

November 4, 2009

Gurgaon

J&K Bank

Structure of Presentation

- Profile of the Bank
- Business Strategy
- Phases of Change
- Performance and Outcome
- Comparative Position

J&K Bank

Basic facts

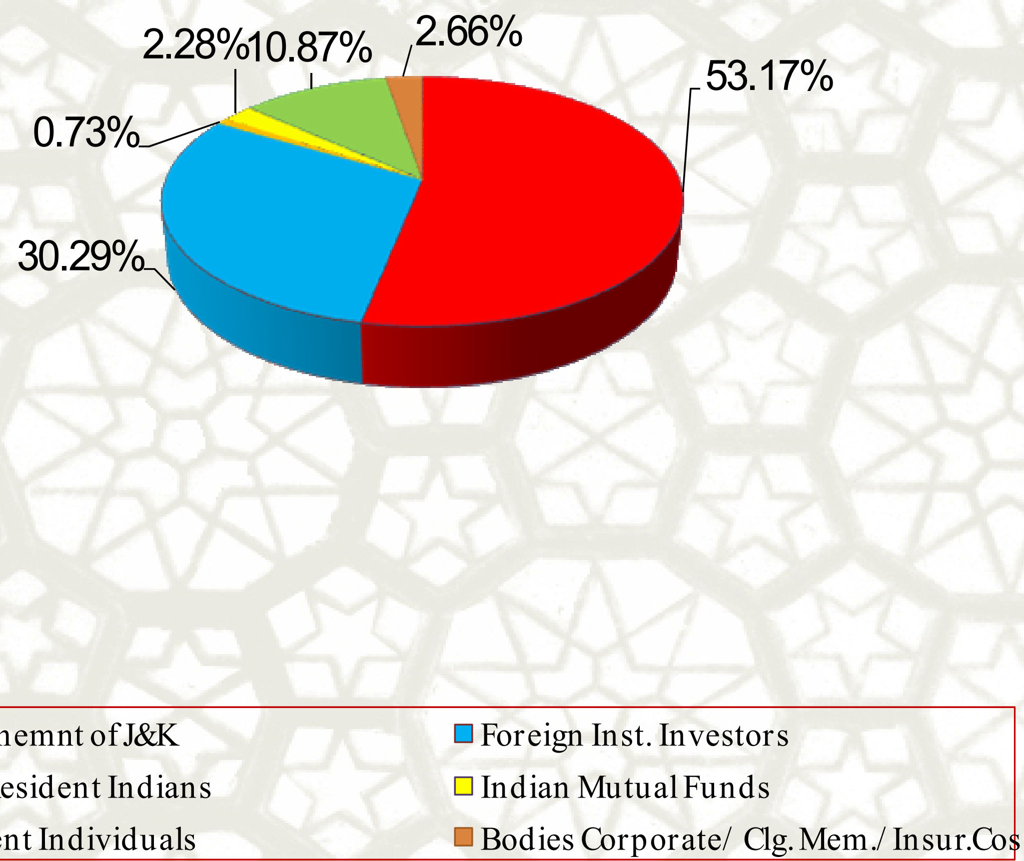
- Incorporated in 1938 as a limited liability company
- Listed on National stock exchange (NSE) and Bombay stock exchange (BSE)
- 53 per cent owned by J&K Government
- Rated "P1 +" by Standard and Poor-CRISIL: highest degree of safety
- Four decades of uninterrupted profitability and dividends

J&K Bank

One of a Kind

- Private sector bank despite government's majority holding
- Sole banker and lender of last resort to the Government of J & K
- Only private sector bank designated as RBI's agent for banking business
- Carries out banking business of the central government
- Collects taxes for Central Board of Direct Taxes in J & K

Shareholding Pattern



As on Oct 23, 2009

J&K Bank

Best of both worlds

- Private Bank despite government's majority holding
- Public ownership:
  - Stability
  - Safety
- Private functioning:
  - Efficiency
  - Growth

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Subsidiaries and Investments

J&K Bank Financial Services Ltd

- Providing Depository Services
- Offering Stock Broking Services

- Insurance JV with MetLife International
- Distributor of
  - Life Insurance products (MetLife)
  - General Insurance (Bajaj Allianz)
- Two Regional Rural Banks

J&K Bank

Business strategy: 2005-2012

- **Two legged business model:**
  - Increase lending in J&K, which is
    - high margin, low volume
  - target niche lending in rest of the country, to
    - Improve margins and build volumes
  - Universal Bank in J&K
  - Specialist bank in rest of the country

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Phase I: Looking inward

- Change in composition of advances
  - In terms of geography – from ROI to J&K
  - In terms of asset types – from low margin to high margin
- A greater focus on liability management
  - Increase low cost retail deposits
  - Increase the maturity structure
- Organizational restructuring

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Phase II: Overhauling outside

- Restructure lending in ROI :
  - Re-pricing
  - Reduce consortium lending
  - Improve WC to TL ratio
- Improve ROI margin by focusing on:
  - Under-serviced areas with high turnover
  - Specialized sectoral lending
  - Specialist branch chain – leather, grains, spices
- Specialist bank in ROI outside

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Phase III: Size and Structure

- Business growth
  - Organic
  - Inorganic
- Focus on size
  - Inorganic growth
  - International foray
- Structural reorganization
  - Towards a conglomerate
  - Investment banking

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Contextual Strategies:

- In the current and emerging environment, what is required is:
  - region-specific credit policies that suit the sub-national growth impulses and context, and
  - productization of finance to suit local enterprises.

(Annual Report 2006-2007)

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Strategic Inference

- Smaller banks — focused and niche players — with regional dominance to outperform.
  - Banking verticals with defined slivers of business
  - Focus on SMEs and the informal segment
- Bi polar structure to emerge
- Muddled middle of the Indian banking sector to get squeezed.

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Advocating Conservatism

"The dangers of managing a business in uncertain environs lie in under estimating the extent and intensity of the downside"

(Annual Report 2007-2008)

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Adapting to Change

- Business model:
  - Flexible
  - Adaptable
- Making liabilities the driver
- Insulate earnings from environment
  - Linking asset to local needs
  - Linking liabilities to local sources

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Results

- Conservatism and consolidation of the last three years has paid off
- The critical choice was not to sacrifice medium to long-term growth to meet a short-term goal, be it business, incomes or profits.
- Our priority is to ensure sustained long-term profitability.

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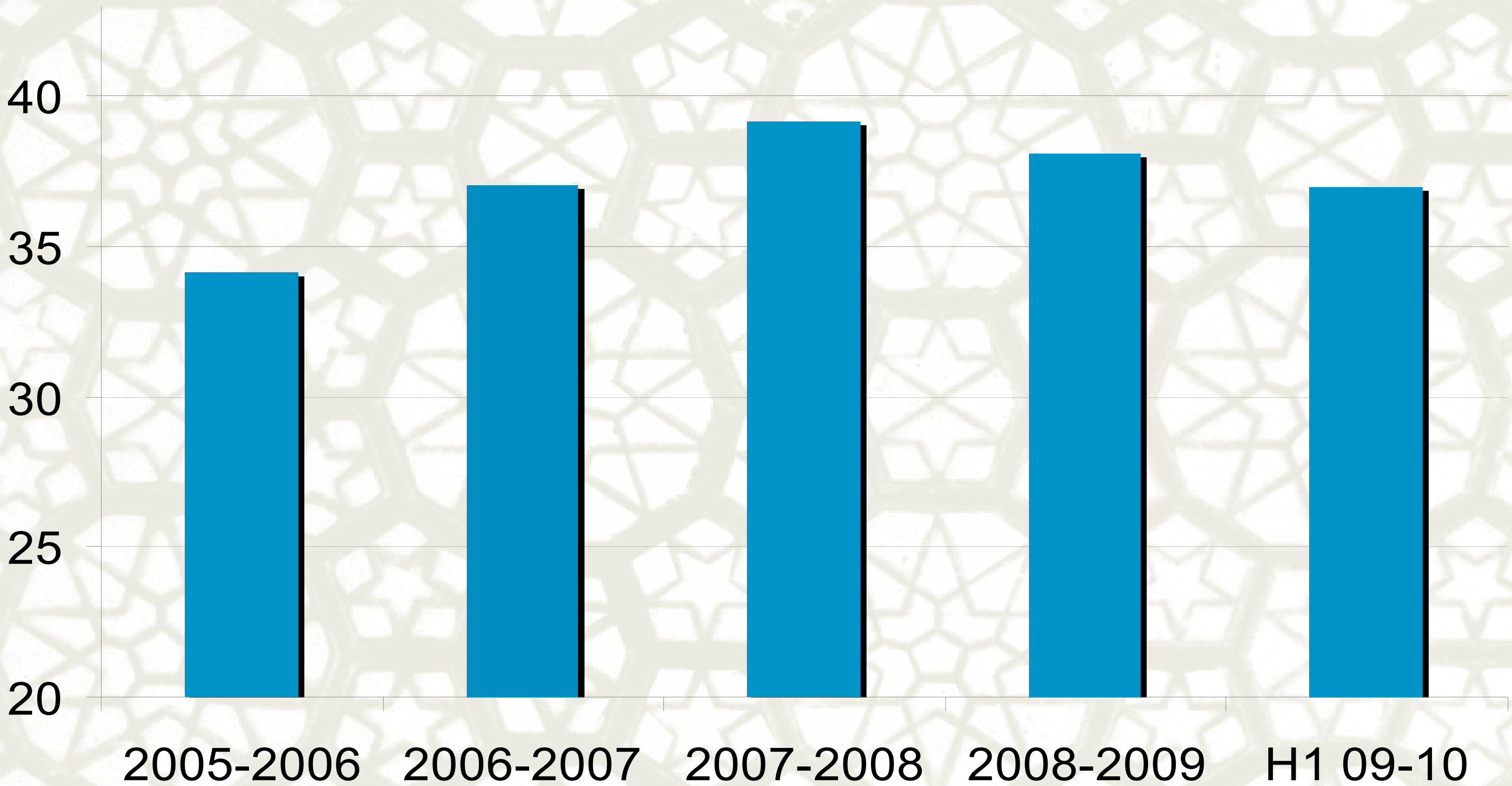
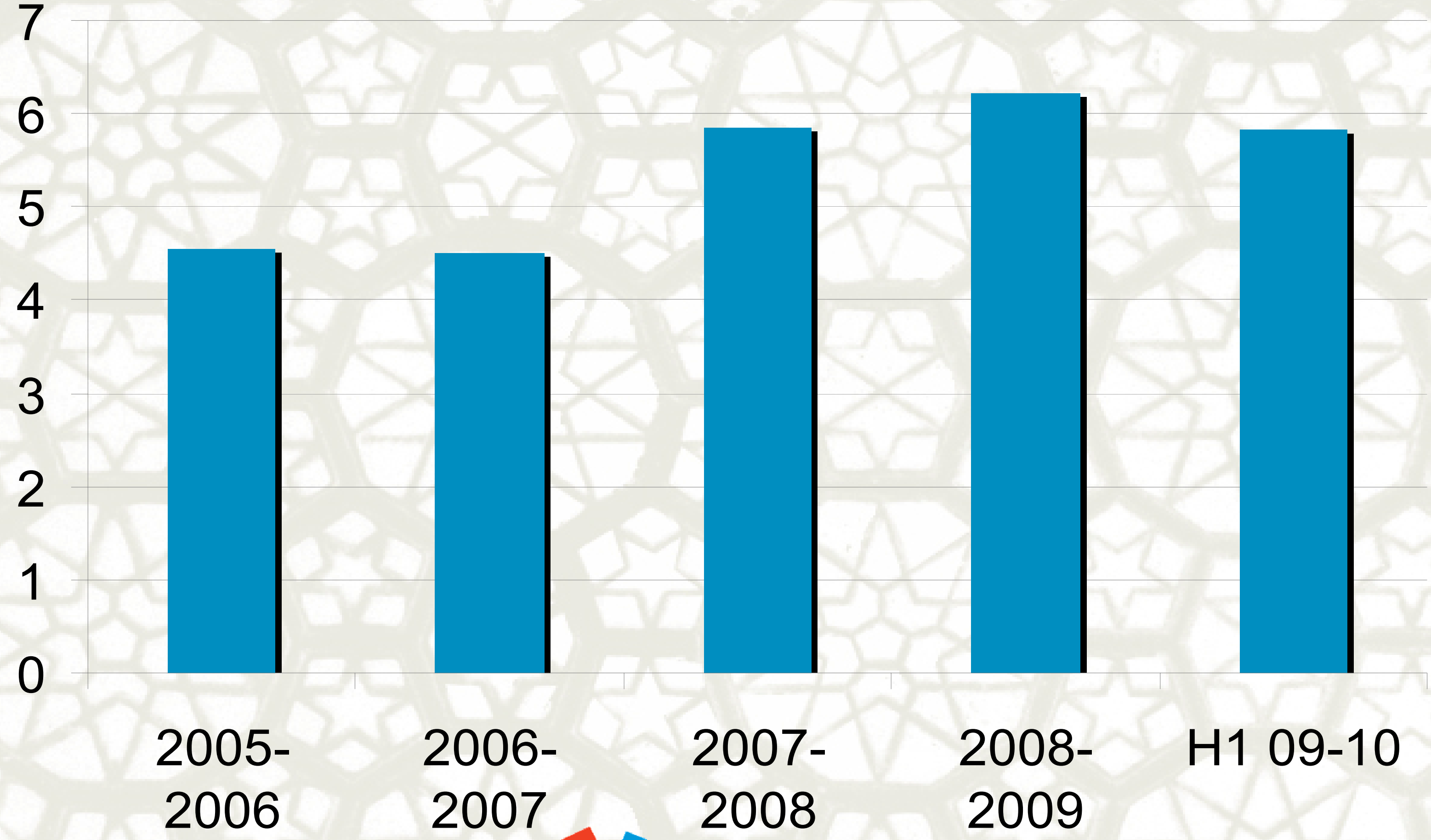
Results

- Despite adverse environment:
  - Earnings are robust,
  - Net interest margins increasing
  - Impairment lower
  - Cost to income reduced
  - Return on Equity rising
  - Return on Assets up and above peer group levels.

Liability Structure : Stable



Cost of Deposits : Contained



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Cost to Income Ratio : Sharp drop

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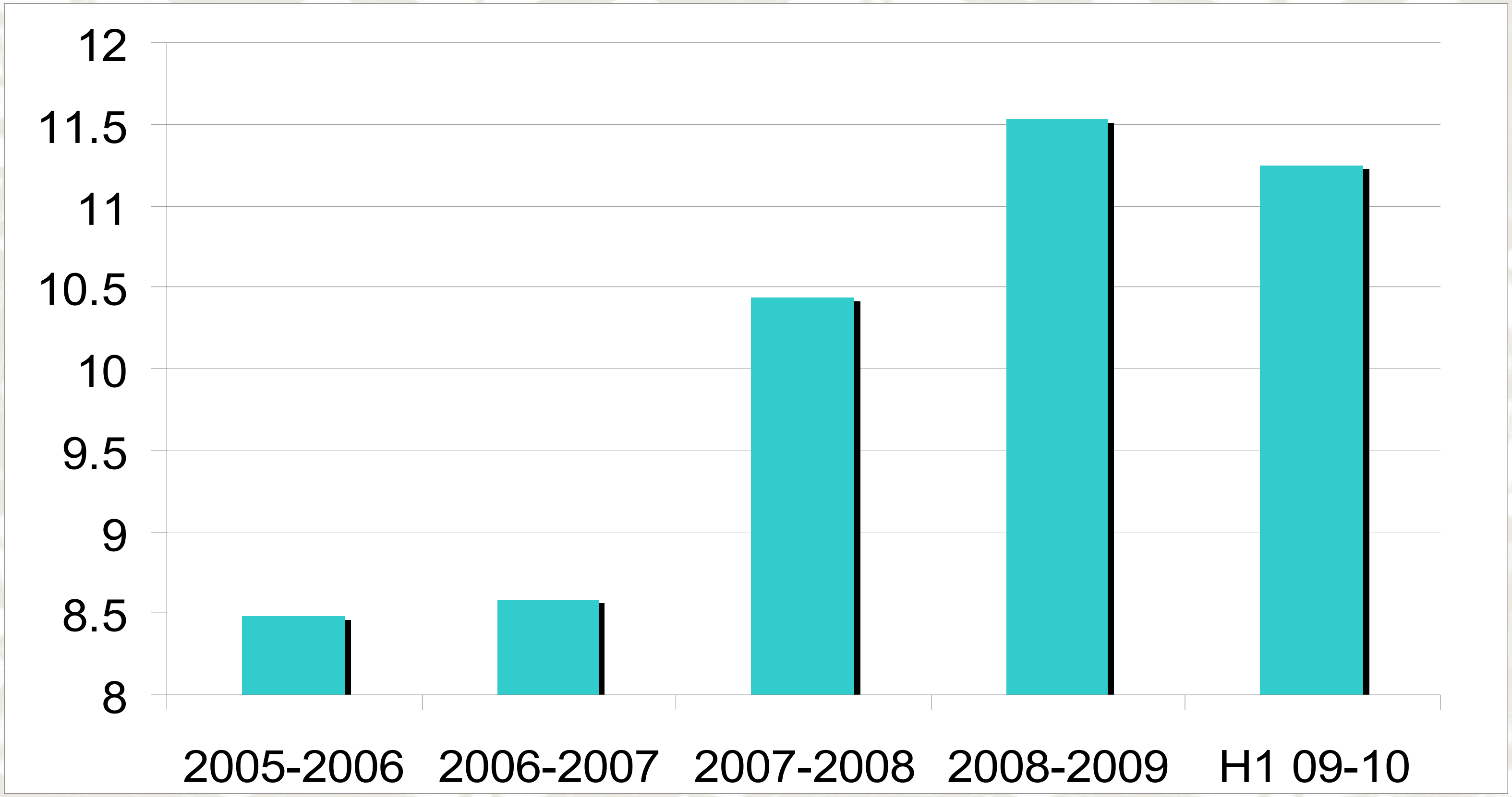
Advances Yield : Increasing



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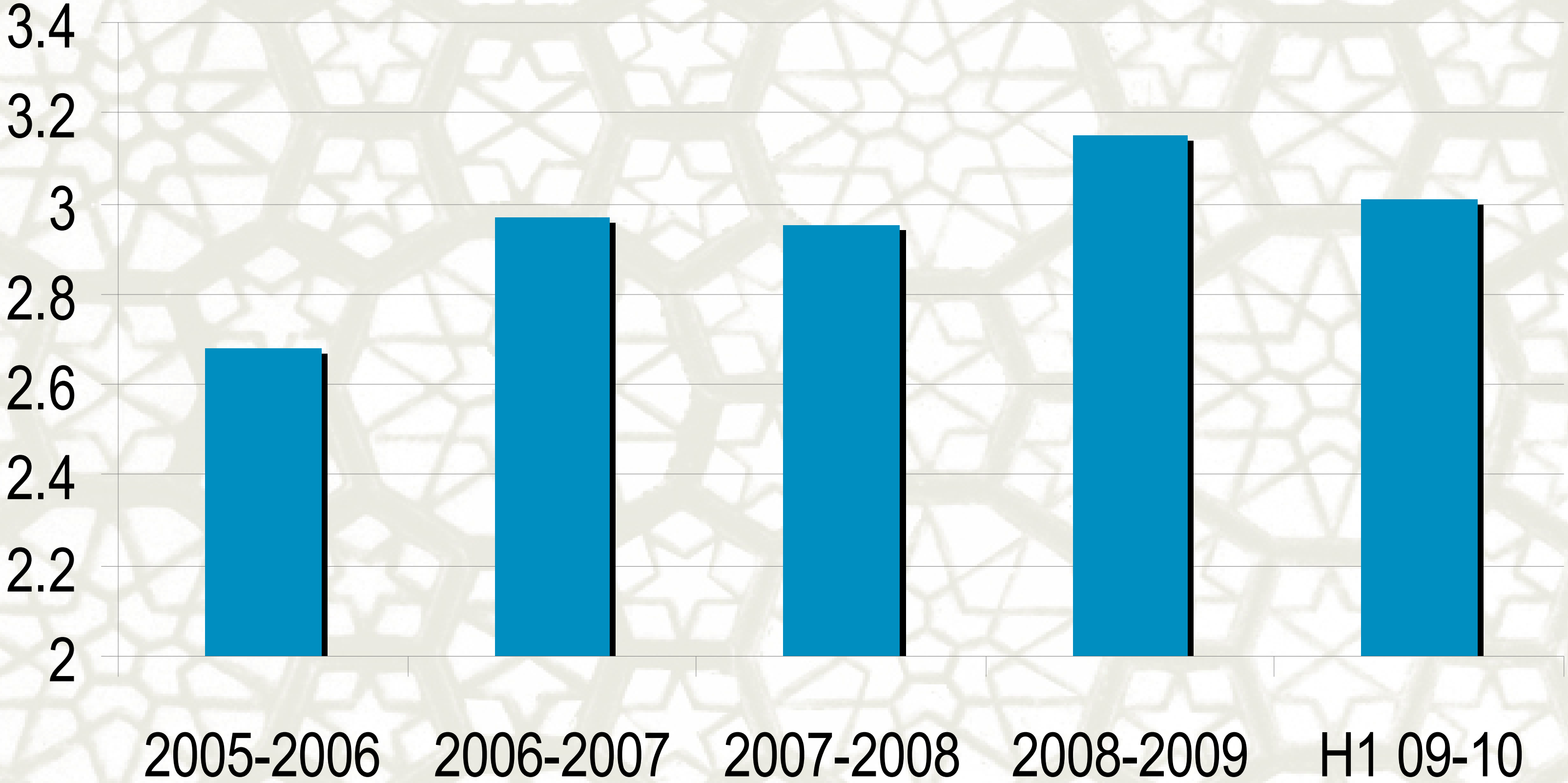
NIIMs : Rising



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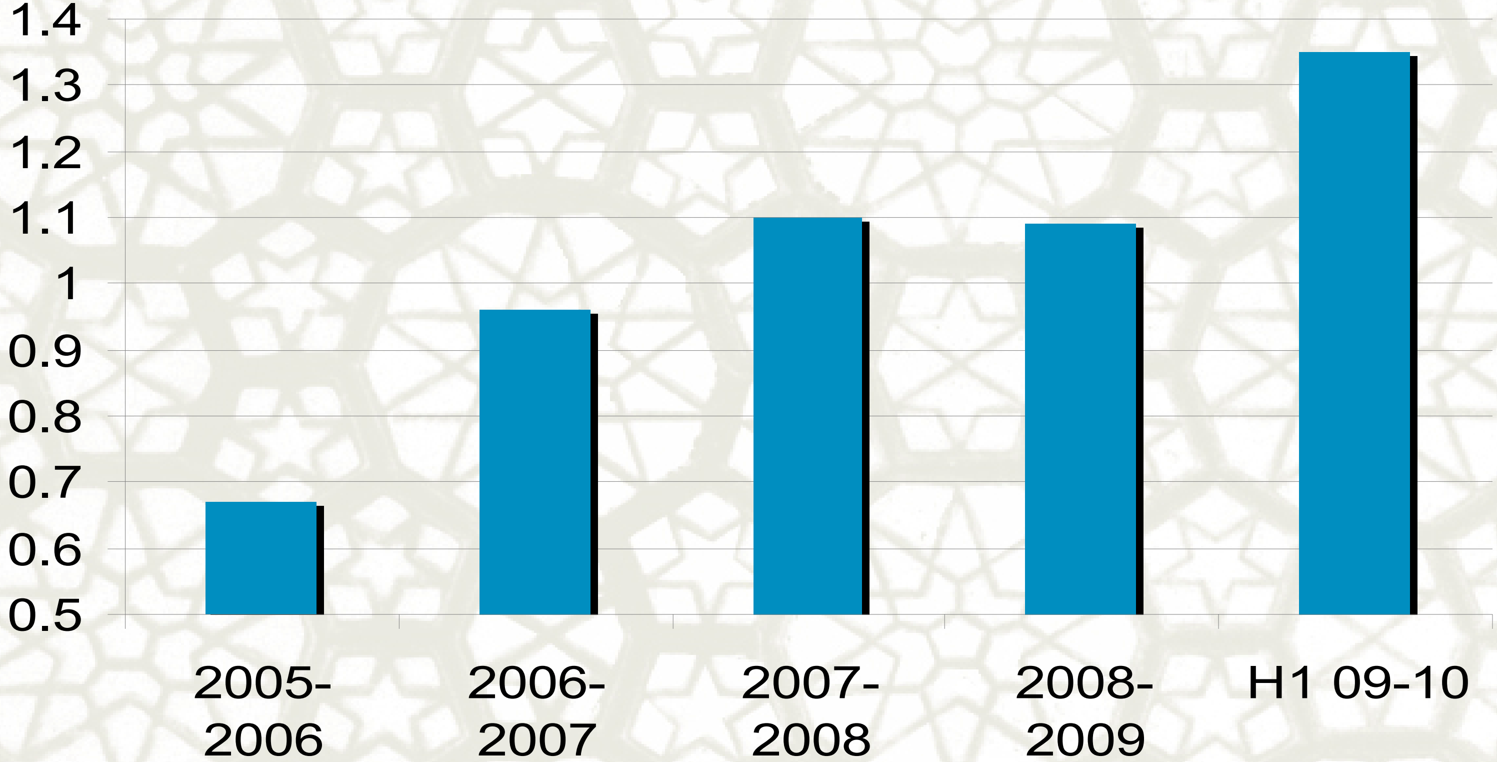
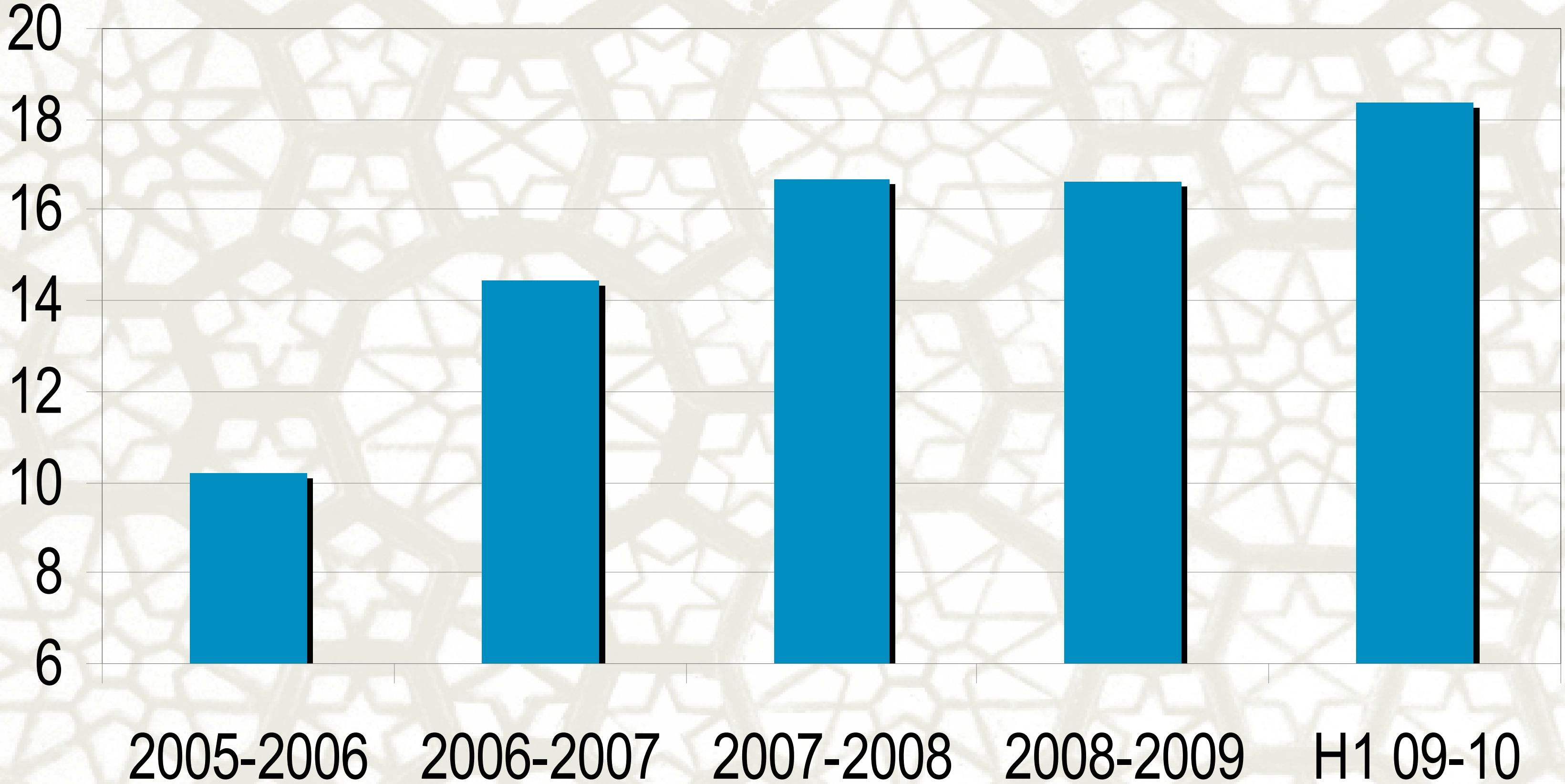
Return on Assets : Constant rise



Return on Equity: On the rise



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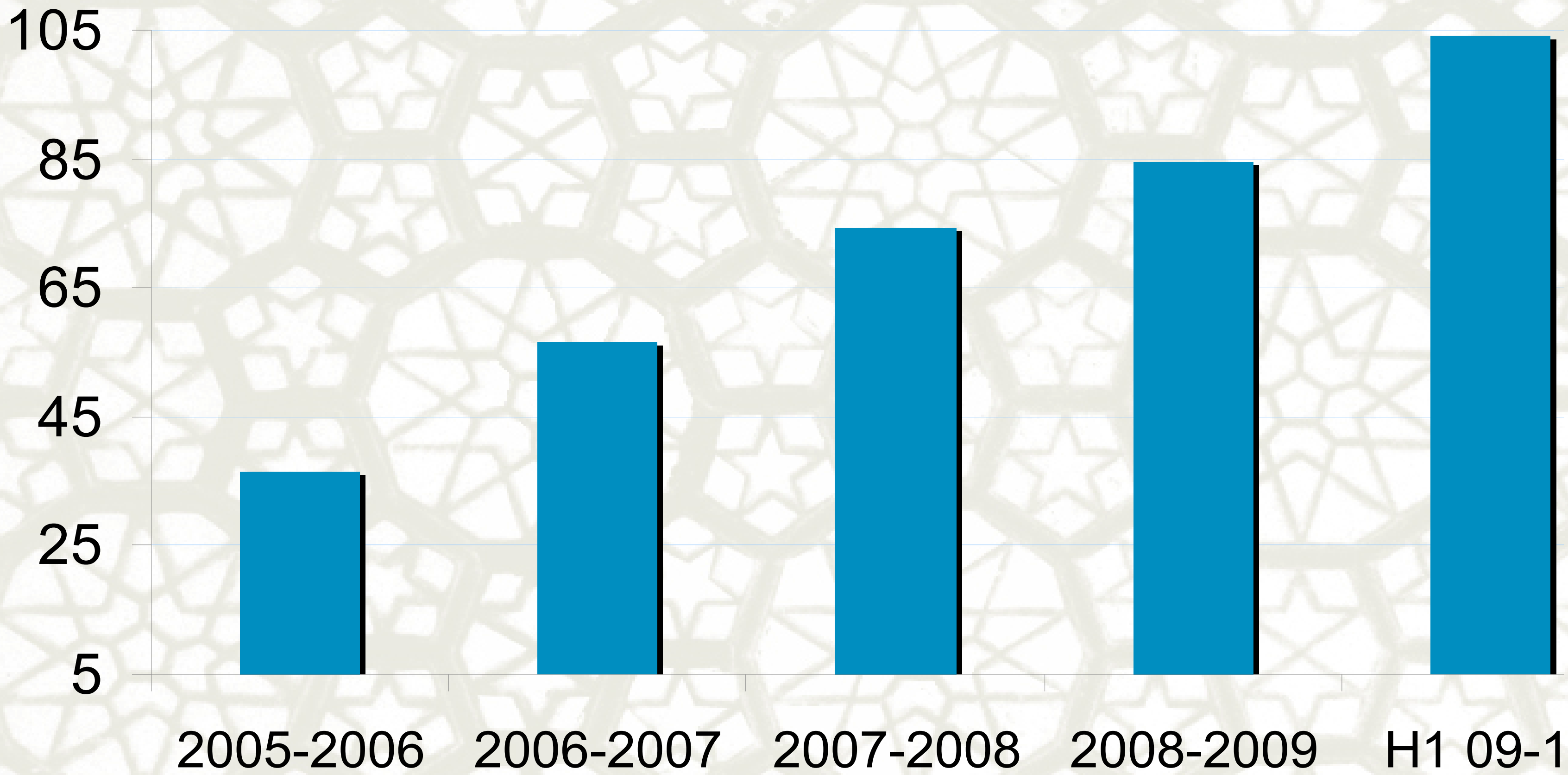
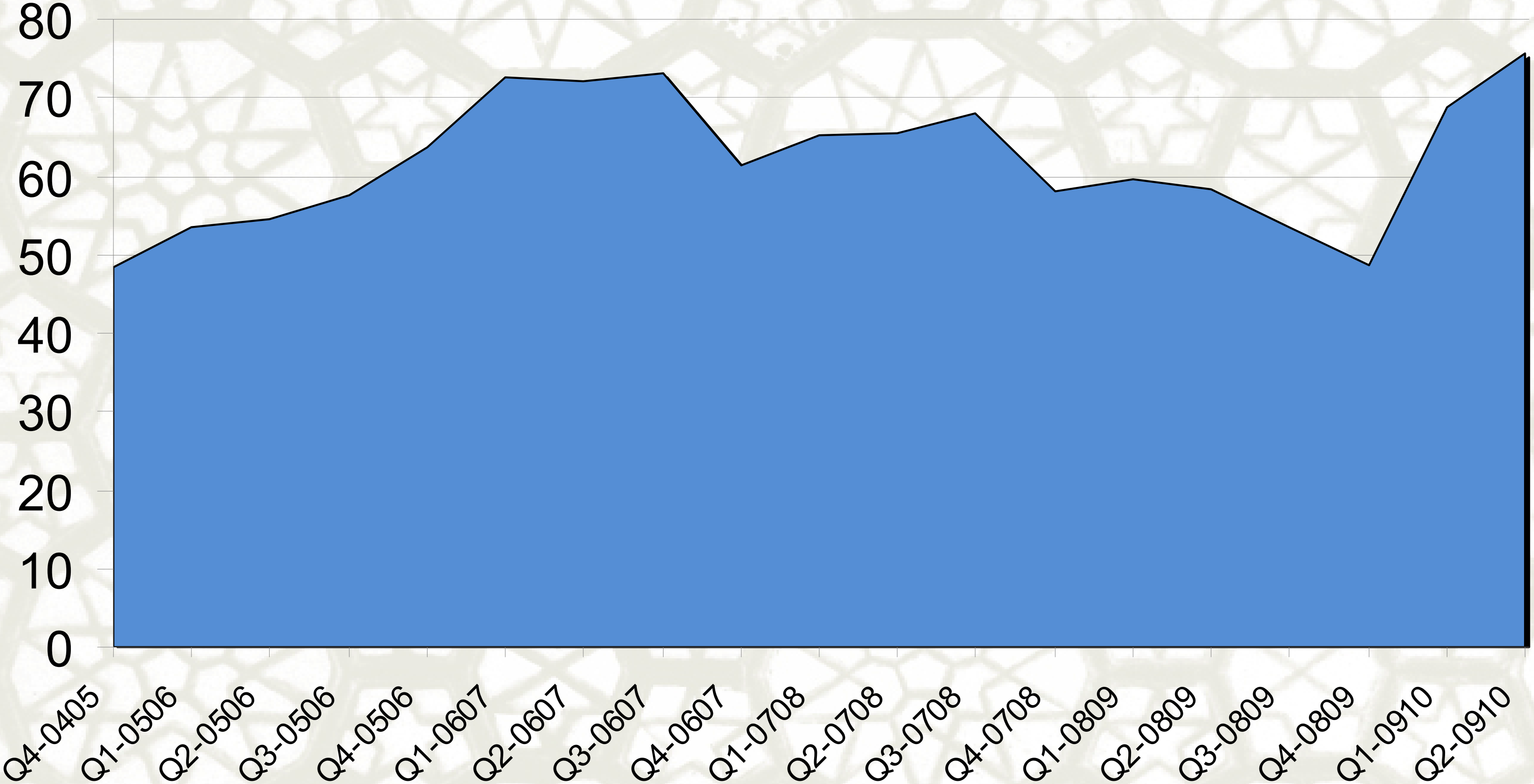
Earnings per share



NPA Coverage: Among the highest



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Financial : Valuation Ratios

	2005-06	2006-07	2007-08	2008-09	H1 09-10
Earning per Share (annualized)	36.48	56.62	74.26	84.54	104.10
Net Asset Value	371.20	414.36	476.28	541.04	593.09
Adjusted Book Value	343.43	374.43	434.30	481.74	568.97
Price to book value ratio	1.23	1.73	1.35	0.91	0.97
Price to adjusted book value ratio	1.33	1.91	1.48	1.02	1.01
Price Earning Ratio (On Ann EPS)	12.50	12.64	8.65	5.80	5.52
Market Cap. To Deposits (%)	9.41%	13.77%	10.89%	7.21%	8.56%
Market price as on date (Rs.)	456.05	715.85	642.10	490.65	574.70
No. of Shares	48477702	48477702	48477802	48477802	48477802

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Profitability Ratios

	2005-06	2006-07	2007-08	2008-09	H1 09-10
Net Interest Margins (%)	2.68%	2.97%	2.95%	3.15%	3.01%
Interest Spreads (%)	2.61%	2.79%	2.64%	2.84%	2.75%
Yield on Advances (Av) (%)(ann.)	8.48%	8.58%	10.44%	11.53%	11.25%
Yield on Investments (Av) (%)(Annualized)	6.22%	6.20%	6.70%	6.79%	5.77%
Cost of Deposits (Av) (%) (annualized)	4.55%	4.50%	5.85%	6.22%	5.83%
Return on Assets (%) (annualized)	0.67%	0.96%	1.10%	1.09%	1.35%
Return on equity (%) (annualized)	10.21%	14.42%	16.68%	16.62%	18.36%
Gross Profit to AWF (%) (annualized)	1.69%	2.02%	2.12%	2.20%	2.55%
Net Profit to AWF (%) (annualized)	0.70%	1.00%	1.17%	1.16%	1.34%

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Asset Quality:

	2005-06	2006-07	2007-08	2008-09	H1 09-10
Gross NPAs (in Rs Cr)	370.19	501.83	485.23	559.27	478.36
Net NPAs (in Rs. Cr)	133.87	193.57	203.55	287.51	116.95
Gross NPA Ratio (%)	2.52%	2.89%	2.53%	2.64%	2.23%
Net NPA Ratio (%)	0.92%	1.13%	1.08%	1.37%	0.55%
NPA Coverage Ratio (%)	63.64%	61.43%	58.05%	48.59%	75.55%
Gross NPA to Net Worth Ratio (%)	20.57%	24.98%	21.02%	21.32%	16.64%

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Operating Ratios:

	2005-06	2006-07	2007-08	2008-09	H1 09-10
Operating Expenses to AWF (%) (ann.)	1.36	1.35	1.31	1.34	1.37
Operating Expenses to Total Income (%)	19.00	18.08	15.06	14.56	14.77
Operating Expenses to Other Income (%)	311.00	232.47	164.73	192.15	117.50
Staff Cost to Total Income (%)	10.59	10.69	8.43	8.62	9.11
Interest Earned to AWF (%)	6.71	6.89	7.93	8.48	8.10
Non-Interest Income to AWF (%)	0.44	0.58	0.80	0.70	1.16
Capital Adequacy Ratio (Basel I)	12.14	13.24	12.80	13.46	13.98
Tier I	11.76	12.60	12.14	12.77	13.39
Tier II	0.38	0.64	0.66	0.69	0.59
Capital Adequacy Ratio (Basel II)				14.48	15.23
Tier I				13.80	14.59
Tier II				0.68	0.64

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Efficiency Ratios:

	2005-06	2006-07	2007-08	2008-09	H1 09-10
Cost to Income Ratio (%)	44.57%	40.13%	38.24%	37.81%	34.92%
CD Ratio (%)	61.67%	67.79%	66.04%	63.42%	64.82%
CASA Ratio (%)	34.17%	37.02%	39.16%	38.11%	36.98%
Business per Employee (In Rs Cr)	5.56	6.17	6.28	7.07	6.91
Net Profit per Employee (In Rs. Lakh)	2.60	4.01	4.76	5.37	6.50
Business Per Branch (In Rs. Cr)	84.56	93.73	93.46	101.19	100.70
Net Profit per Branch (In Rs. Lakh) (Annualized)	39.40	60.86	70.87	76.89	94.68

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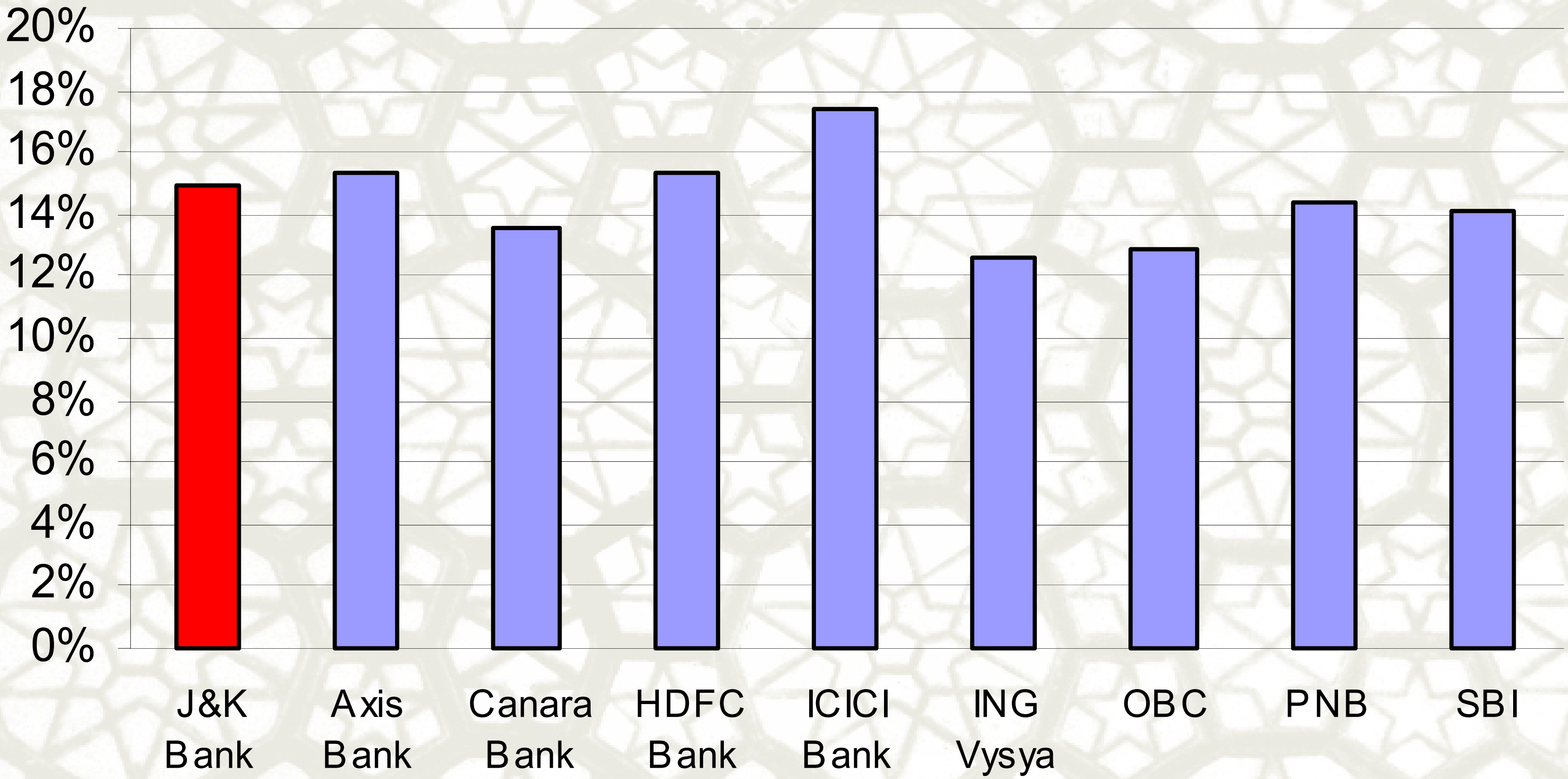
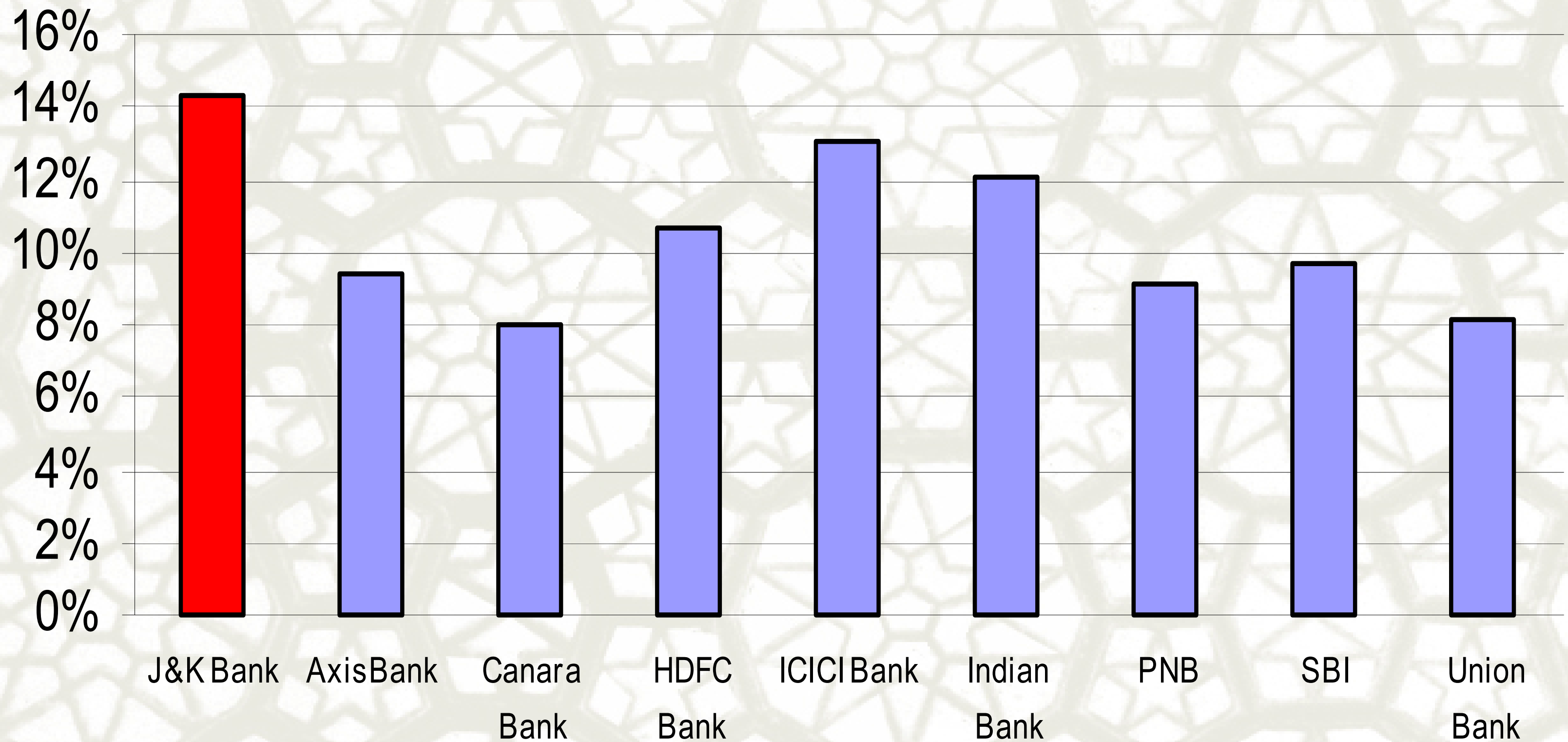
Capital Adequacy Ratio – Basel II



As on June, 2009

Higher Tier I Capital (Basel II)



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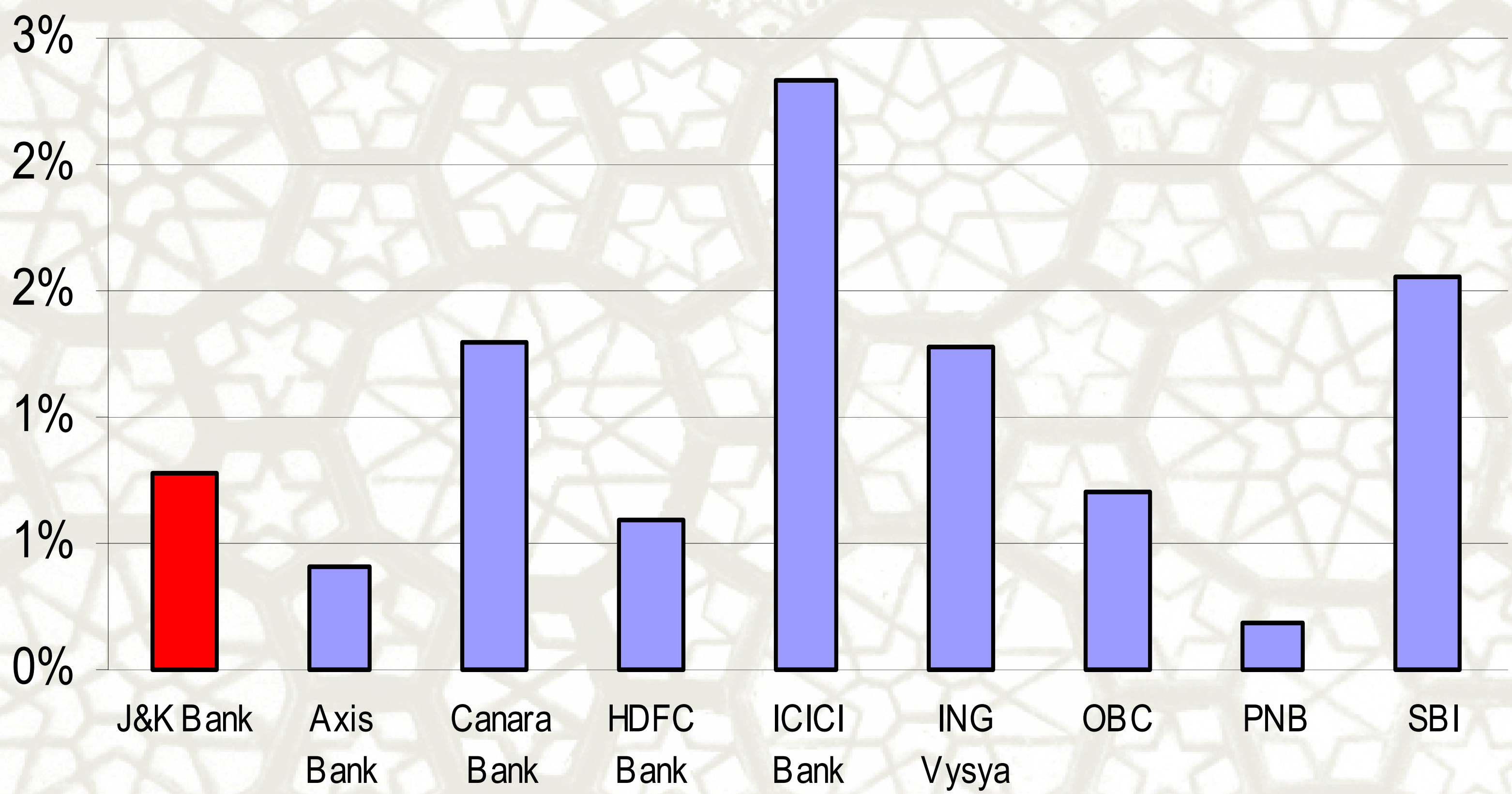
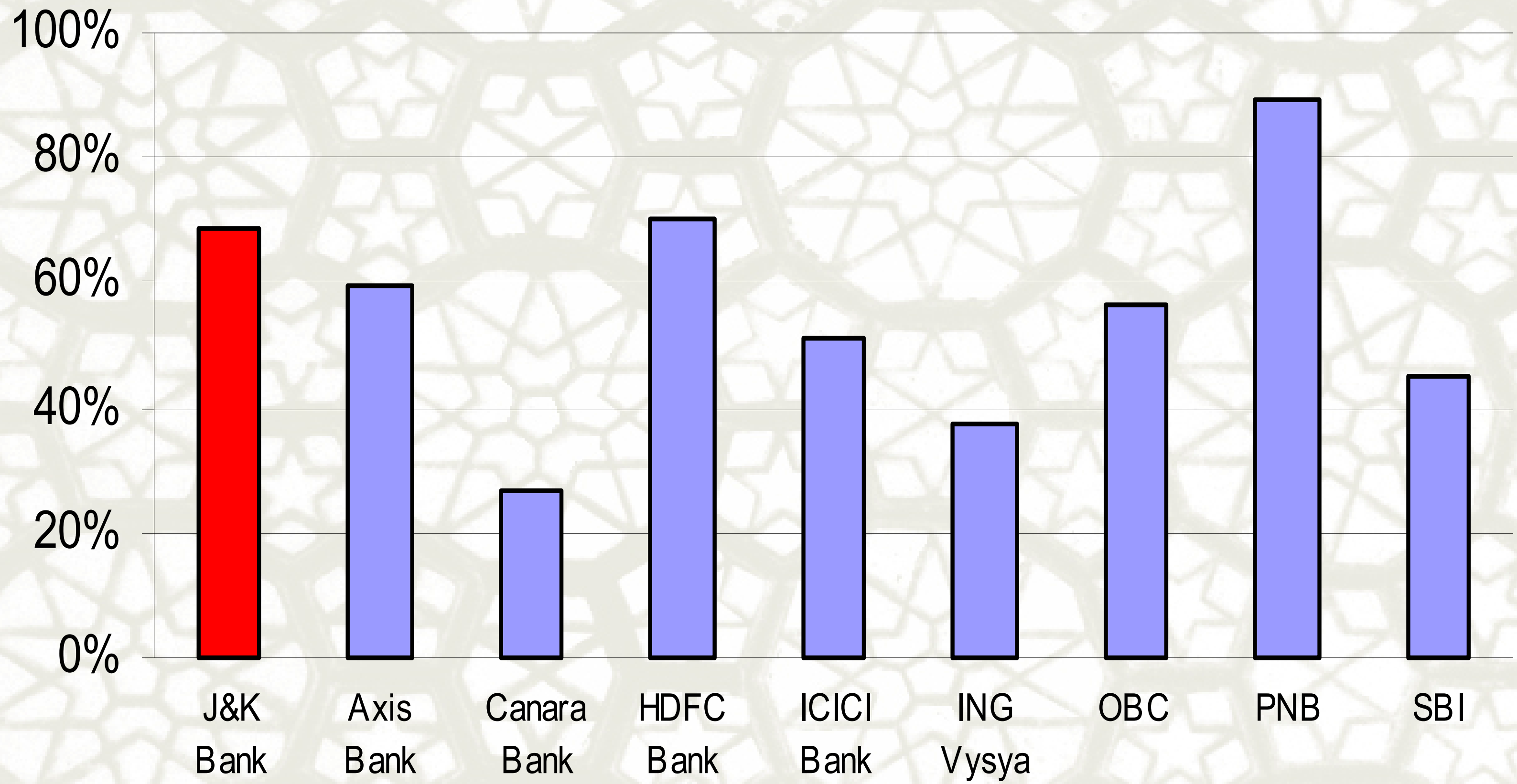
Net Impaired Loans



As on June, 2009

Coverage Ratio



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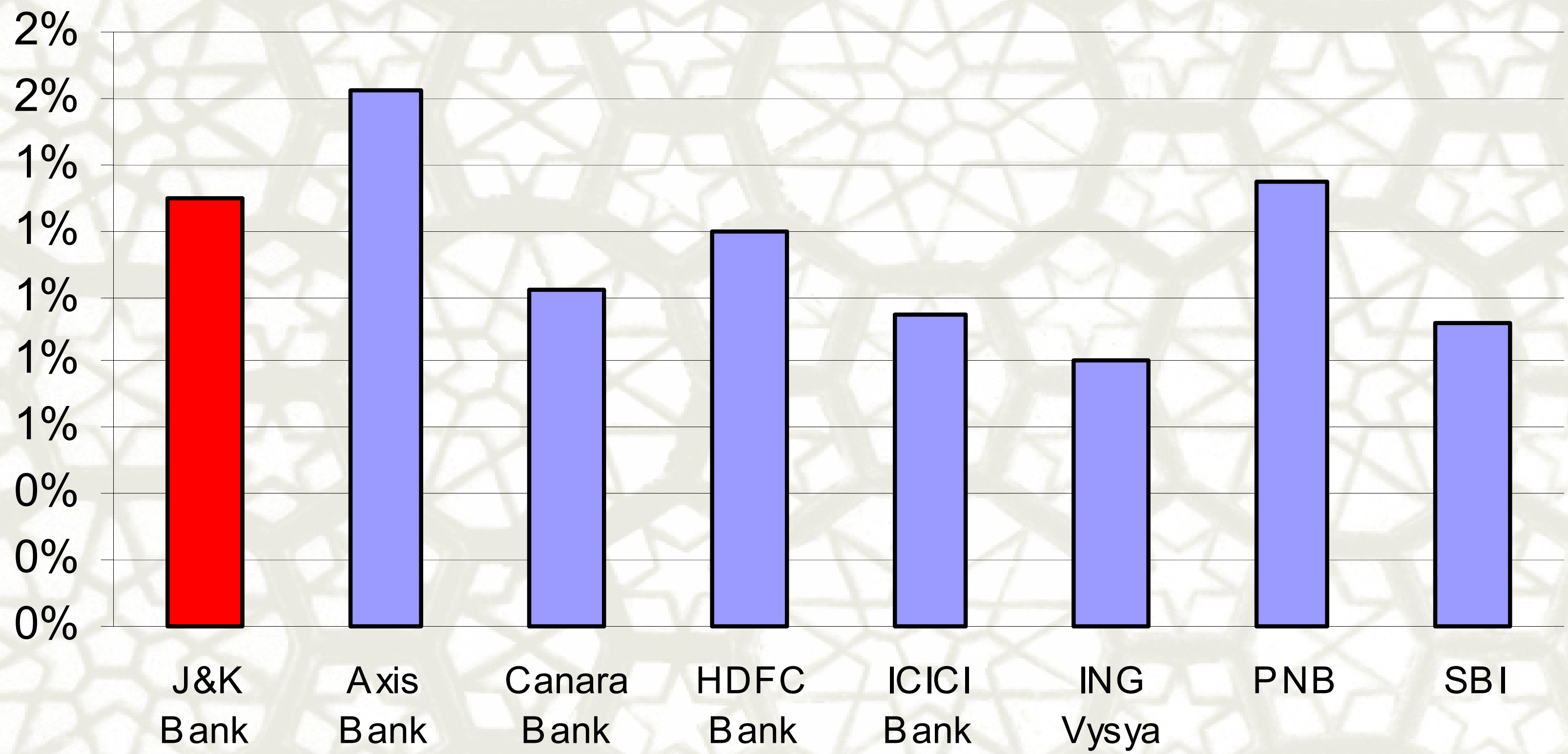
RoA (Annualized)



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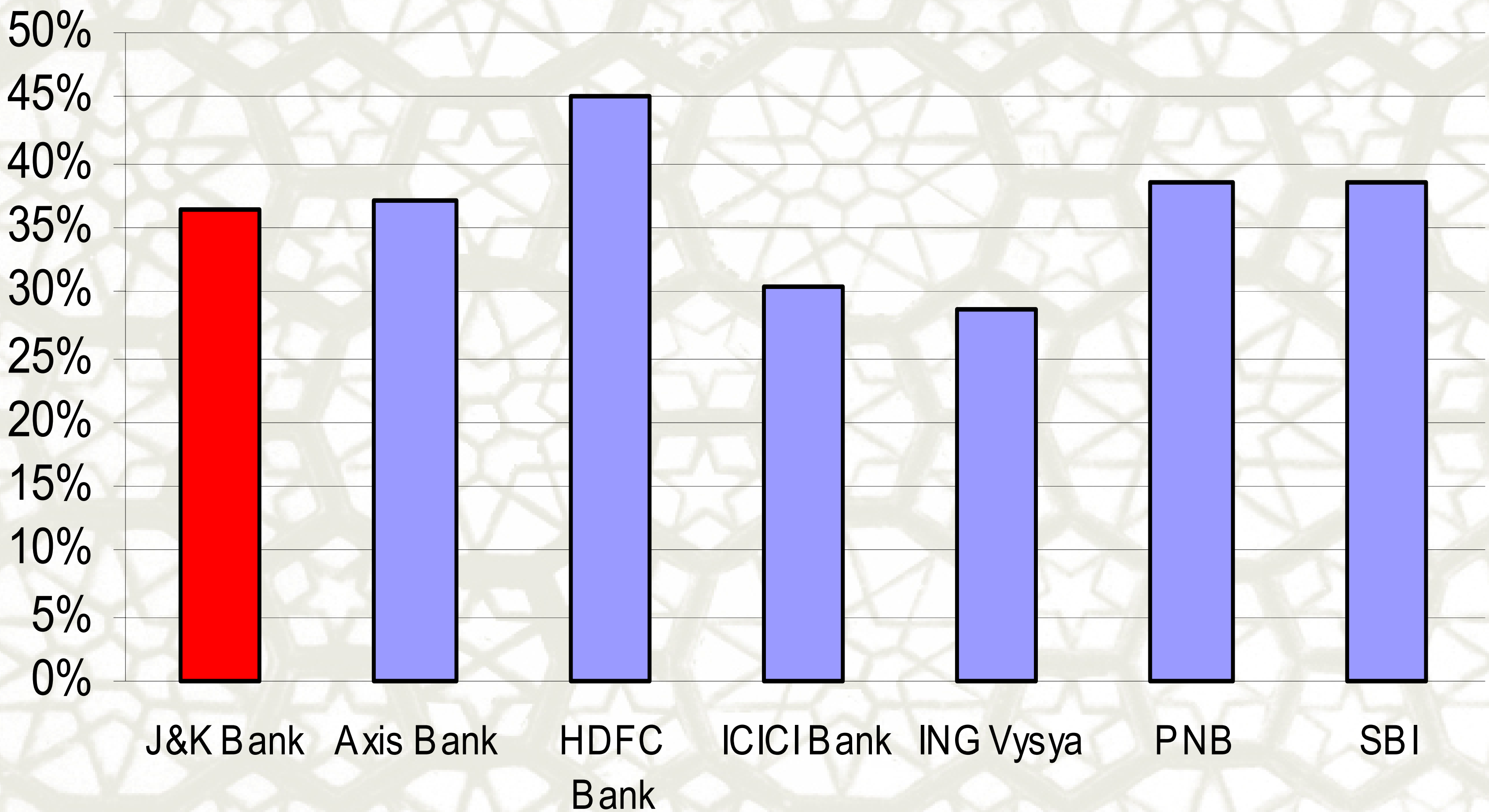
CASA Ratio



As on June, 2009

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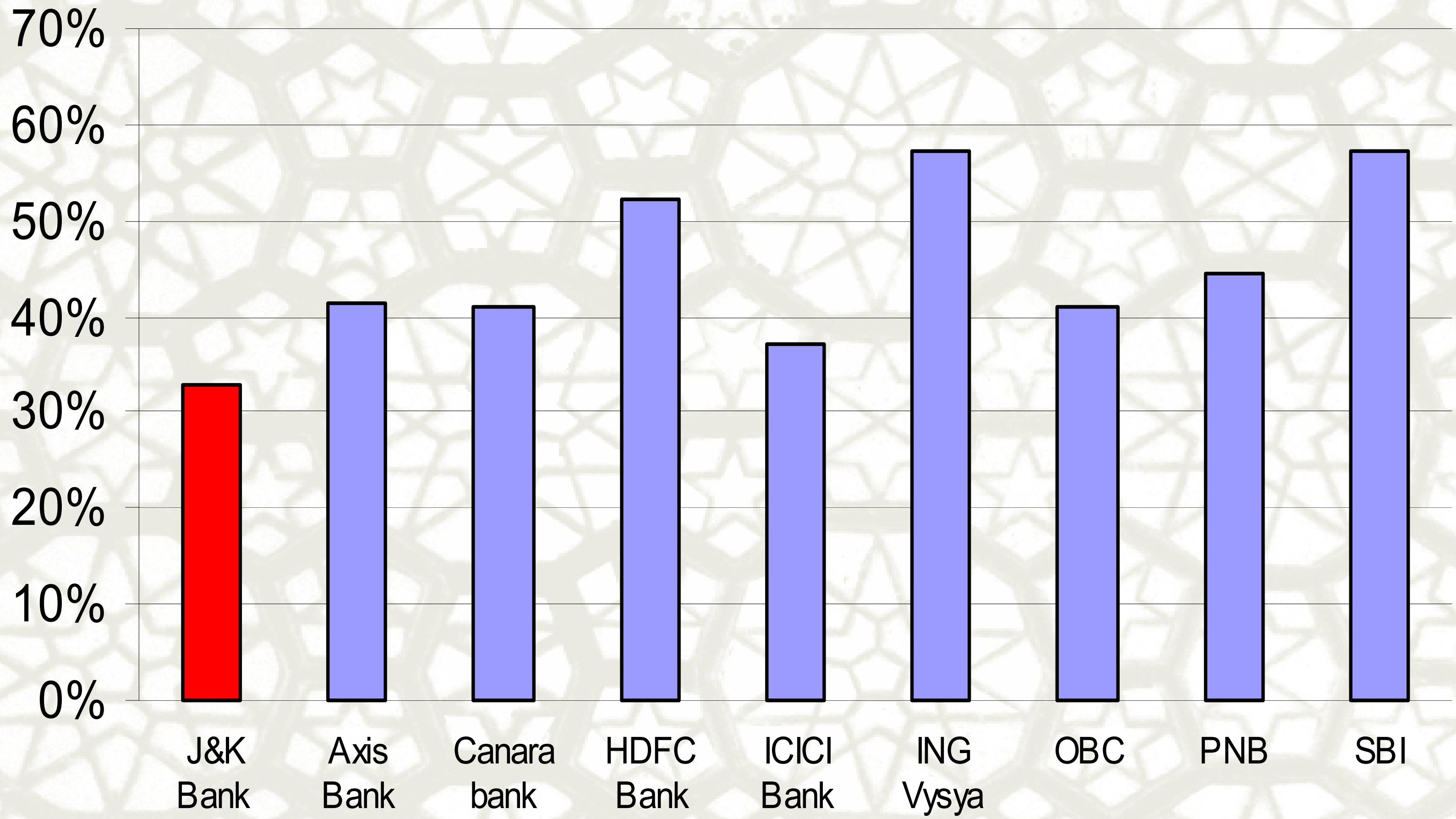
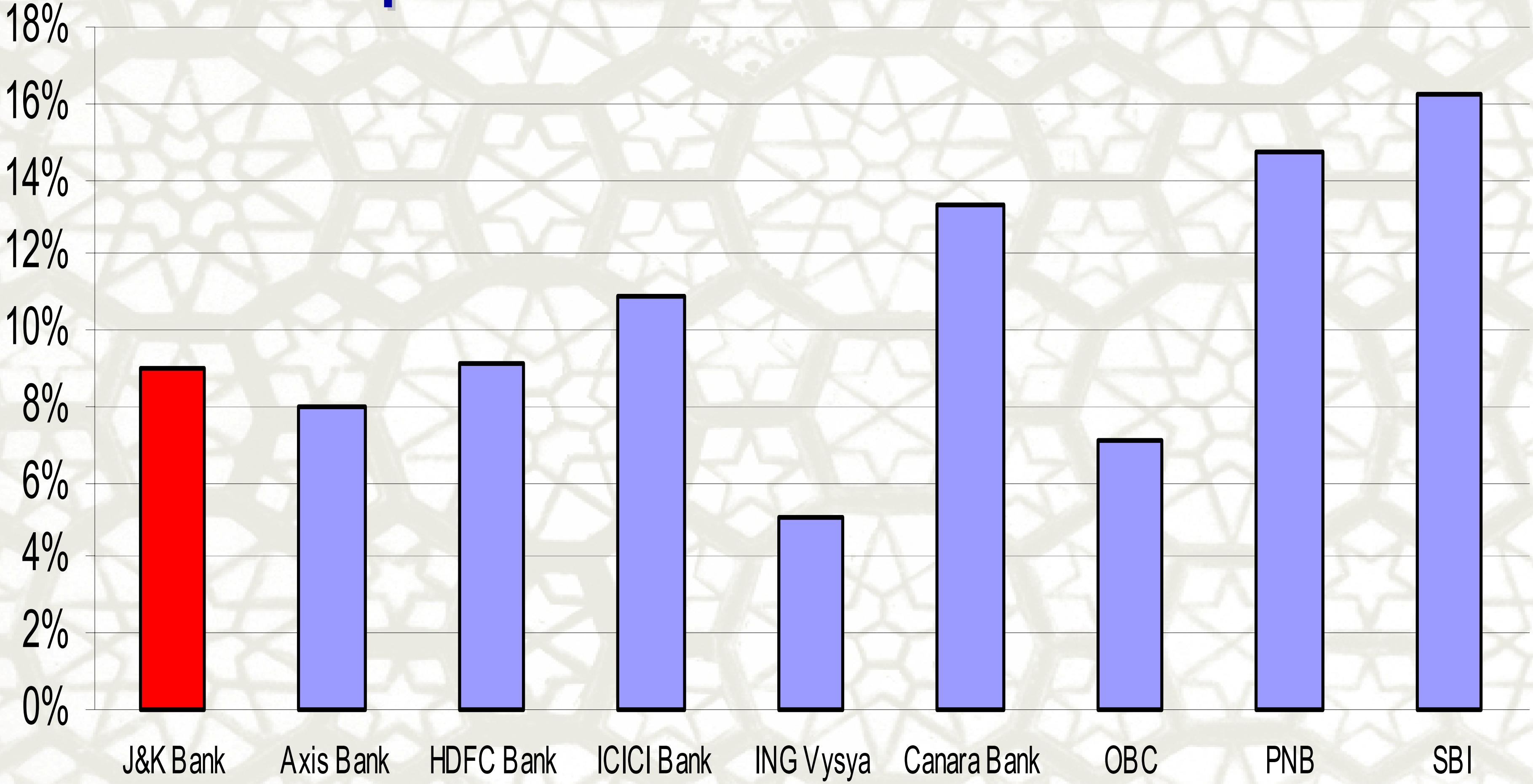
Cost to Income



As on June, 2009

Staff Expenses to Total Income



As on June, 2009

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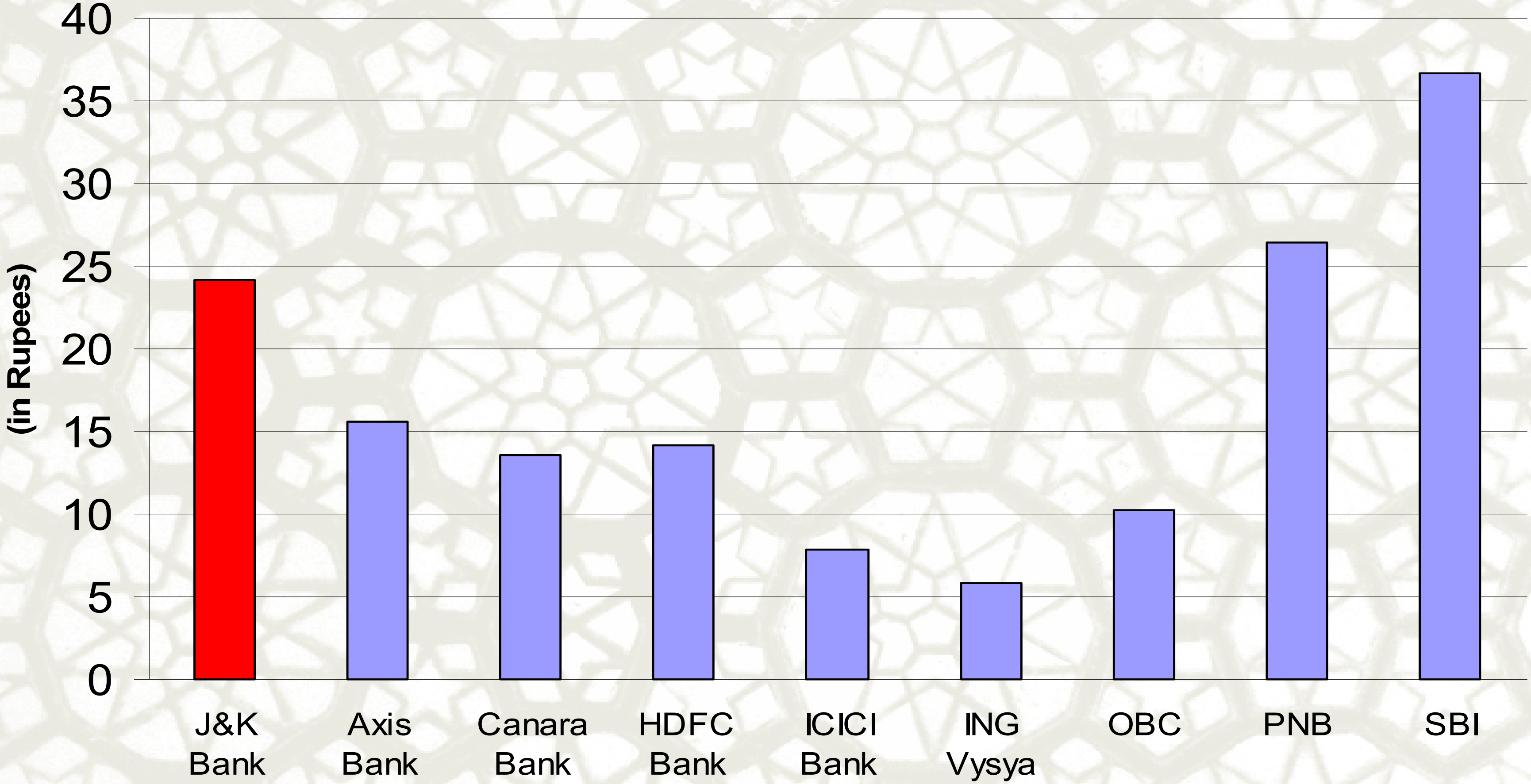
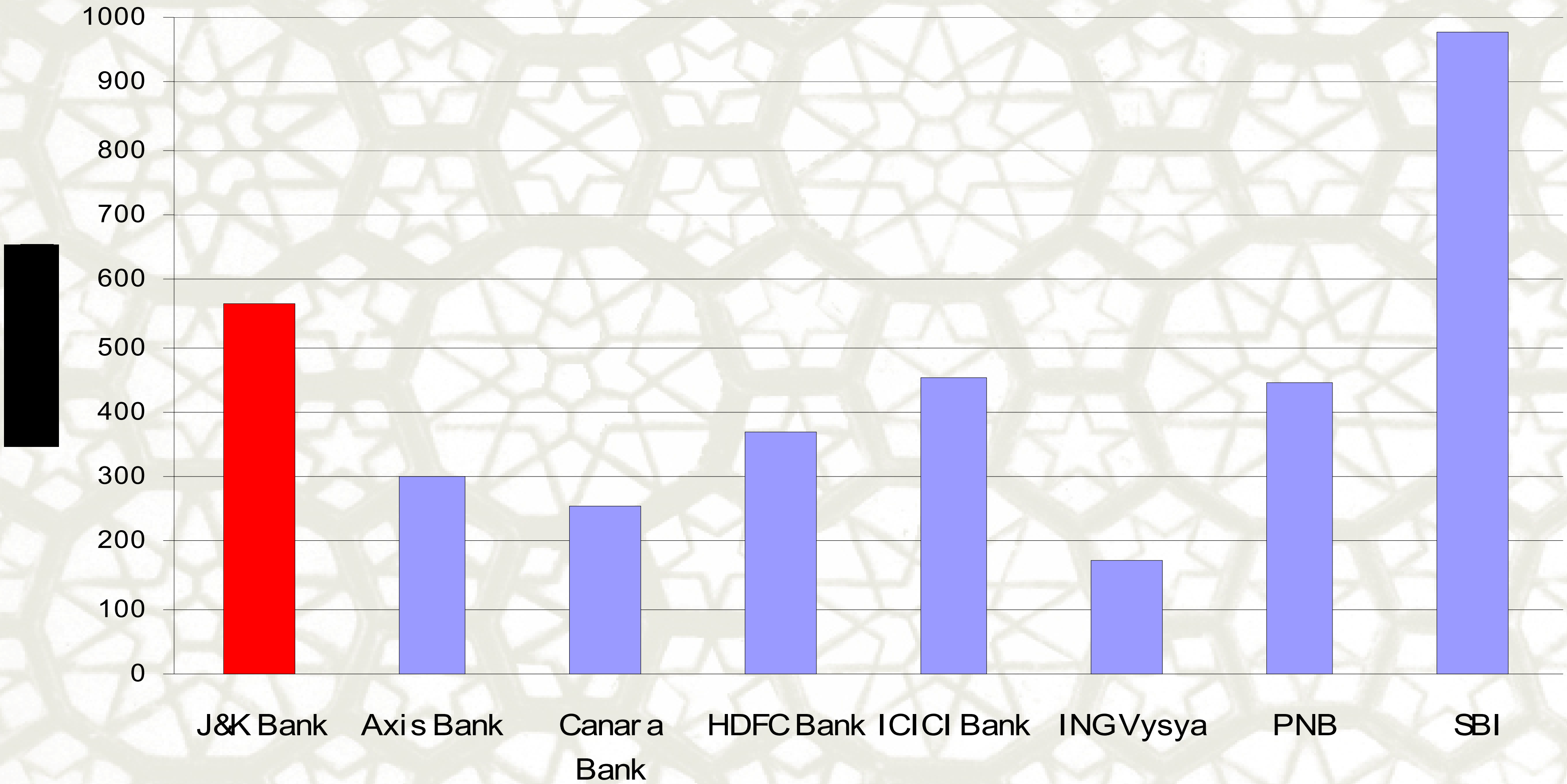
Earnings per Share



As on June, 2009

Book Value



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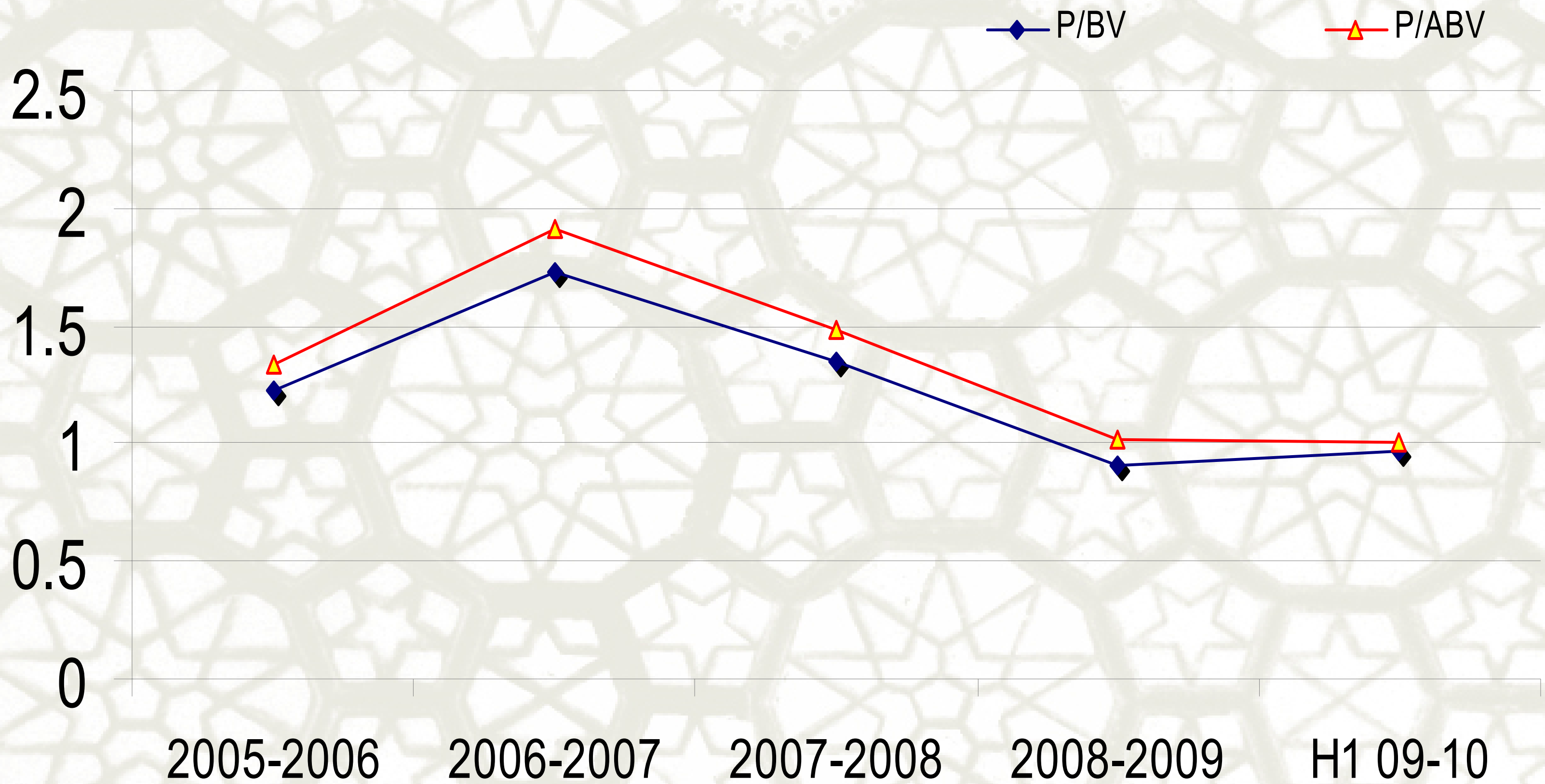
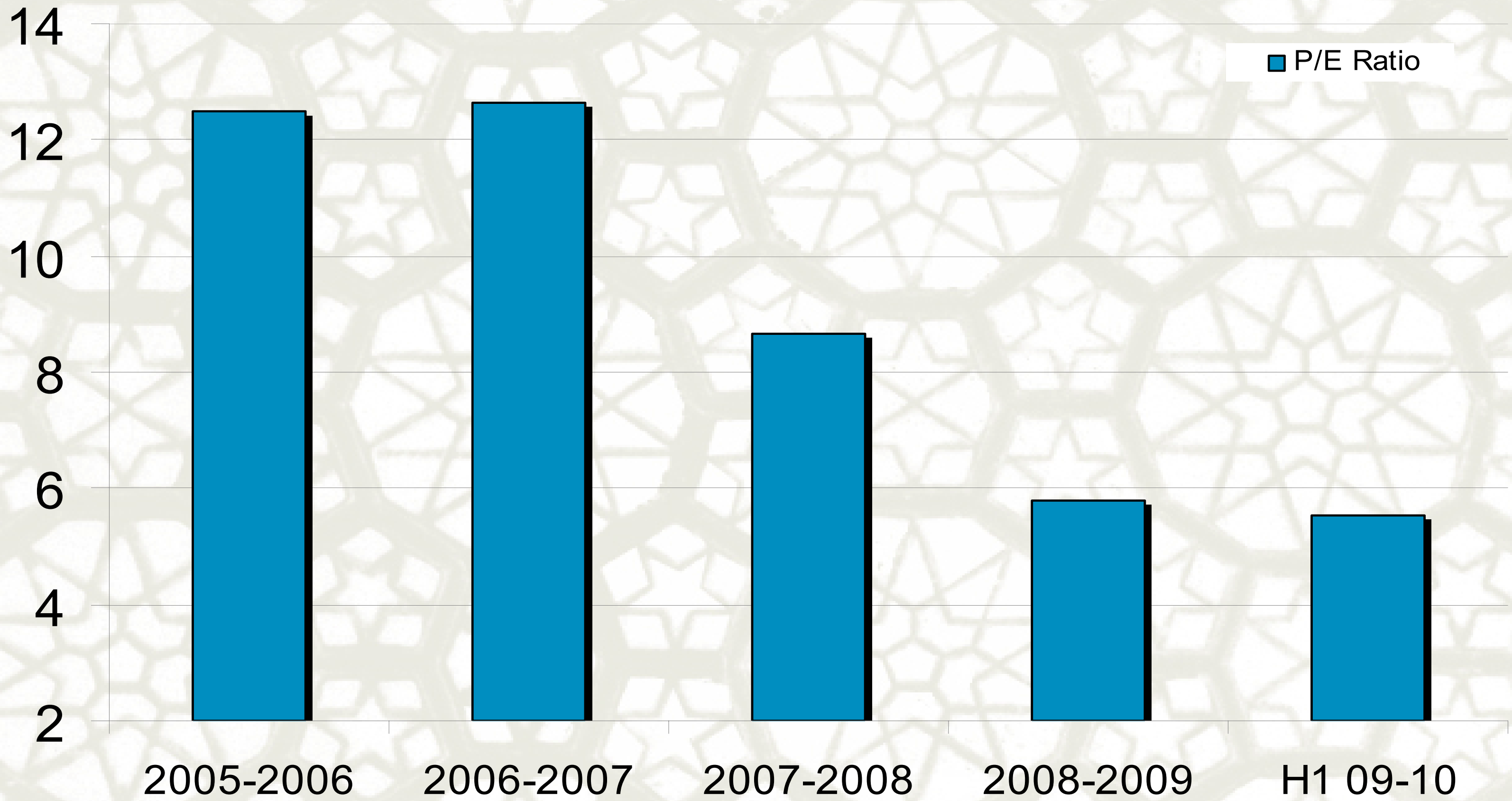
The "Kashmir" question!

(Price/Book Value Ratio and Price/Adjusted Book Value Ratio)



The Puzzle!



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Recap

- J&K Bank will outperform the sector
- With rising margins and lower costs, even as
- Economic growth in India declines and
- Banking sector slows down in uncertain environment and wavering policy prescriptions

Thank you!

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