Management Discussion and Analysis

Global Growth Forecast to Rise Further in 2018 and 2019

At the global front, year 2017 was marked by a number of key structural initiatives to build strength across macro-economic parameters for sustainable growth in the future. The growth in the first half of the year suffered despite global tailwinds. However, the weakness seen at the beginning of 2017, bottomed out as 2018 set in. The economy seems to be on the path to recovery, with indicators of industrial production, stock market index, auto sales and exports having shown some uptick. Global growth for 2017-18 is now estimated at 3.9 percent (higher than projected). Upside growth surprises were particularly pronounced in Europe and Asia but broad based, with outturns for both the advanced and the emerging market and developing economy groups exceeding the forecasts by 0.1 percentage point. The stronger momentum experienced in 2017 is expected to carry into 2018 and 2019, with global growth revised upwards for both years. For the two-year forecast horizon, the upward revisions to the global outlook result mainly from advanced economies, where growth is now expected to exceed 2 percent in 2018 and 2019. This forecast reflects the expectation that favorable global financial conditions and strong sentiment will help maintain the recent acceleration in demand, especially in investment, with a noticeable impact on growth in economies with large exports.

One of the major positives over the past few years has been the declining inflation levels. Consumer price inflation has in fact, fallen to multi year lows during the last fiscal. This has been possible on account of falling or stable global commodity prices and better management of supply shortages in the agrarian economy. That said, reversal of inflationary pressures during the latter part of 2017 as crude oil prices have started moving up and favourable base effects have waned. Prior to this period, some increase in food prices along with one-time modifications on account of pay revisions in the public sector and housing rent allowance being revised upwards had led to rising inflation. The latest reading for Feb'2018 saw larger than expected easing that came on the back of a slowdown in the more volatile food price inflation. Also, only marginal uptick in core inflation was recorded possibly on the back of lower base effect and a likely pass-through of input costs.

As per IMF, the growth forecast for the United States has been revised up given stronger than expected activity in 2017-18, higher projected external demand, and the expected macroeconomic impact of the tax reform, in particular the reduction in corporate tax rates and the temporary allowance for full expensing of investment. Growth rates for many of the euro area economies have been marked up, especially for Germany, Italy, and the Netherlands, reflecting the stronger momentum in domestic demand and higher external demand. Growth in Spain, which has been well above potential, has been marked down slightly for 2018, reflecting the effects of increased political uncertainty on confidence and demand. While stronger oil prices are helping a recovery in domestic demand in oil exporters, the fiscal adjustment that is still needed is projected to weigh on growth prospects. Growth this year and next is projected to remain above 2 percent in the Commonwealth of Independent States, supported by a slight upward revision to growth prospects for Russia in 2018.

The main challenges for the FY 2018-19 are likely to come due to rising crude oil prices on account of global oil output cuts. The expected global macroeconomic effects account for around one-half of the cumulative upward revision to the global growth forecast for 2018 and 2019, with a range of uncertainty around this baseline projection.

Outlook for Asia

Asia is expected to continue to lead the world in economic growth with exports enjoying increased demand as a result of stronger global economic growth, which will support higher output in South Asia and the Association of Southeast Asian Nations (ASEAN). The aggregate growth forecast for the emerging markets and developing economies for 2018-19 is unchanged, with marked differences in the outlook across regions. Emerging and developing Asia is expected to grow at around 6.5 percent over 2018–19, broadly the same pace as in 2017. The region continues to account for over half of world growth and this growth is expected to moderate gradually in China, pick up in India, and remain broadly stable in the ASEAN-5 region. China's One Belt One Road initiative to expand infrastructure links will likely continue to improve efficiencies and connectivity in the pan-Asian economy, promoting economic expansion in the medium term. India and China are expected to do very well, with projected average annual economic growth rates. This robust growth is a result of relatively competitive business environments compared with other emerging markets, favorable demographics in most of these countries, and strong integration in the global value chain.

India's Outlook 2018-19

India's economic performance remained promising for FY 2017-18, however, there was a setback to the sentiment in February 2018 on account of fraud of around ` 14000 Crore involving multiple banks particularly PNB. This prompted RBI to take several preventive measures like, directing banks to discontinue the practice of issuance of LoUs/LoCs for Trade Credits for import into India by AD-Category banks with immediate effect. Banking Industry as a whole took a jolt due to this incident and the repercussions thereof on several banks.

Despite this, the economic outlook is expected to strengthen further in FY 2018-19 on the back of political stability. The biggest challenges for FY 2018-19 are as to how the economy can maintain its recovery in the face of increasing inflationary pressures, coupled with a higher fiscal deficit as well as an increasing debt burden. The key to this conundrum lies in the revival of consumer demand and private investment.

Reserve Bank of India (RBI) is optimistic that the economy would outpace China to become the world's fastest growing major market this year and help lure investors seeking opportunities. RBI recently increased the repo and reverse repo rates by 25 basis points for the first time since January 2014, because of rising inflation. The central bank has now projected inflation for the FY 2018-19 at 4.8-4.9% in the first half and 4.7% in the second half of the year. Further, RBI undertook corrective measures directing banks to strengthen the inspection and audit systems, investigate bad loans above 50 crores and reconcile their Swift Messaging Procedure by integrating Swift Operations with core banking solutions to impart visibility to swift transactions. This shall catalyze investments and demand which were hit by demonetization in third quarter of FY 2016-17, implementation of the Goods and Services Tax (GST) last year and the trust deficit arising out of the multi-billion fraud in PNB at the beginning of year 2018. It will boost the general market sentiments and bond markets in particular. Moreover, slowing inflation, accelerating growth and an economy that relies on domestic consumption may help cushion India from the escalating trade war between the U.S. and China. The Reserve Bank has forecast the $2.3 trillion Indian economy will expand 7.4 % in the financial year 2018-19.

- During the Financial Year 2017-18, India's economic performance was quite a subject of interest. While the first quarter of the year saw the impact of demonetisation settling down, in the next quarter, introduction of the landmark Goods and Services Tax (GST) brought in some uncertainties as businesses adjusted to the new regime. This did not take long, and from the third quarter onwards, signs of growth returning were evident.
- For the FY2018-19 as global economic activity continues to strengthen, global growth is forecast to grow by 3.9% during 2018 as per the International Monetary Fund's (IMF) January 2018 World Economic Outlook. The IMF expects India to grow at 7.4% during 2018 which could increase further to 7.8% during 2019 in contrast to 6.7% during 2017. The Economic Survey for 2017-18 pegs the figure at 7-7.5% for the financial year ahead.
- As per the second advance estimates of national income released by the Central Statistics Office in February 2018, real Gross Domestic Product (GDP) at constant prices is estimated to grow at 6.6% for 2017-18. The Indian economy achieved an impressive growth rate of 7.2%, a five-quarter high during the third quarter (Oct-Dec) of FY18 as opposed to 6.5% in the second quarter. However, in view of change in RBI's recent monetary policy, GDP in India is expected to grow at 7.5% to 7.6% in the first half and 7.3% to 7.4% in the second half of FY 2018-19.

J&K Economy Survey

The Gross State Domestic Product (GSDP) of J&K State at constant (2011-12) prices for the year 2017-18 is estimated at ` 109136.52 crore, as against the estimate of Rs 100597.57 crore for 2016- 17, indicating growth of 8.49 per cent during 2017-18. At current prices, GSDP for 2017-18 is estimated to be Rs 140886.76 crore as against the estimate of ` 126230.91 crore for 2016- 17, showing an increase of 11.61 per cent during the year. The projected estimates for the year 2018-19 at constant (2011-12) prices and current prices of GSDP is Rs 116637.44 crore and Rs 157383.77 crore.

The projected growth for the year 2018-19 is roughly estimated at 6.87%. The share of product taxes in total Gross State Value Added (GSVA) at basic price for the year 2016-17 and 2017-18 is 10.50% and 11.02% respectively. The share of product subsidies in total Gross State Value Added (GSVA) at basic price for the year 2016-17 and 2017-18 is 2.10% and 1.95% respectively.

The Central GST Act 2016 was passed by the Parliament in the present form and was notified by Government of India on 12th April 2017 which was applicable to whole of India except state of Jammu and Kashmir, as the powers to tax in J&K State are enshrined under Section 5 of J&K state constitution. Presidential orders were passed on 08-07-2017 where under CGST and IGST were made applicable to J&K State w.e.f. 08-07-2017. With the implementation of GST, Banking industry was faced with both challenges as well as opportunities. The challenge of compliance with the painstaking one-time process of registrations, training of human resources & increased rates for availing banking services and the opportunity to augment the loan portfolio and indirect collection of taxes on behalf of customers.

Total expenditure for 2018-19 is estimated to be Rs 80,313 crore, a 15.2% increase over the revised estimates of 2017-18. In 2017-18, there was a decrease of Rs 9,744 crore (12.3%) of expenditure in the revised estimates over the budget estimates. Total receipts (excluding borrowings) for 2018-19 are estimated to be Rs 71,180 crore, an increase of 14.4% as compared to the revised estimates of 2017-18. In 2017-18, total receipts fell short of the budgeted estimate by Rs 3,553 crore. Revenue surplus for the next financial year is targeted at Rs 13,084 crore, or 8.3% of the state Gross Domestic Product

(GDP). Fiscal deficit is targeted at Rs 9,673 crore (6.1% of state GDP). Primary deficit is targeted at Rs 4,948 crore (3.1% of state GDP). The departments of Power, Home, Education, Health and Medical Education saw the highest increase in allocations creating another opportunity for Banks.

Banking system overall in the state has exhibited remarkable operational as well as institutional growth over last two decades. The institutional structure of banking system in J&K consists of multiple market players viz. Commercial Banks, Regional Rural Banks and Co-operative Banks. The settlement of large amounts of pending NPA accounts is more likely now and the amount of NPAs is also expected to improve during the current financial year.

J&K Bank – Performance and Prospects

The Jammu and Kashmir Bank posted an operating profit of `1381.87 Cr for FY 2017-18. The bank ended the year with a net profit of ` 202.72 Cr. Net NPA ratio of the bank stood at 4.90 pc as against 4.87 pc a year ago. Net Interest Margin improved to 3.65 pc from 3.38 pc reported in last FY ended March 31, 2017. The total business of the bank reached Rs 1.37 lakh Cr registering an increase of ` 14640 Cr over the business a year ago. In line with the Bank's focus about consolidation and strengthening of the Bank's Balance Sheet, the emphasis during the last financial year was on arresting the slippage of advances, recovery of NPAs and consolidating the NPA coverage ratio. The NPA problem in J&K Bank is being contained now and the situation is coming under control.

The strategy of instilling transparency and faith in the system adopted by the new regime continued in the current year. Given the deployment of funds towards provisions in FY 2017-18, the requirement of provisions for incremental NPAs recognized during the year would be substantially less than what the Bank actually provided for during the year. The Provision Coverage Ratio of the Bank has been maintained at 65.83 pc from 66.88 pc as on March 31, 2017. The Standard Loan Book and Investment Book of the Bank now is mostly high rated and the woes of asset quality issues in this portfolio are assumed to be passé. The Bank recorded deposit growth of 10% and gross advances growth of 10% during the year.

Continuing with proper liability management and management's decision of non-rollover of high-cost bulk deposits kept the CASA ratio of the Bank at 50.89 pc as on March 2018 from 51.70 pc a year ago. The Bank is operating with a better than industry-average NIM of 3.65 pc which is bound to improve further going forward. A YoY credit growth of 14.25 pc is indicative of growth momentum setting in. Efforts of Impaired Assets Portfolio Management vertical too has brought about a substantial improvement in reduction/ recovery of bad loans to the tune of ` 3098 Cr during FY 2018. Bank's superior franchise in its home state as evidenced by its dominant market share of over 60 pc in loans and deposits continues and is expected to be reinforced further with adoption of a plan based strategy of outgrowing the market. The state contributes more than half of the loan portfolio, 86 pc of overall deposits and 93 pc of CASA deposits of the Bank.

The State government being the promoter and major stake holder is committed to support the envisaged business growth of the Bank by augmenting the capital base of the Bank. Jammu and Kashmir Government infused capital of ` 532 Cr in the FY 2016-17 and 2017-18, which further strengthened the capital position of the Bank. Prior to capital infusion, Government had a share holding of 53.17% in the Bank and post infusion, share holding of Government has gone to 59.23%. Board/Shareholders have already conveyed their approvals for raising proportionate amount of capital from public/institutions through QIP route. In addition, Board has already approved raising of Basel III compliant ATI capital of ` 1000 Cr and Basel III compliant Tier II capital of ` 1000 Cr in FY 2018-19. The capital augmentation through such infusion and envisaged retained earnings over the ensuing periods shall help in complying with the regulatory capital adequacy requirement and support envisioned credit growth.

The Bank has roped in professional consultants for drawing a medium-term business plan with strategy for achieving the targeted goals, suggesting re-engineering of business processes focusing on improving efficiency and cutting wastages, ensuring high level of regulatory compliances and realigning HR policies to support the business plan achievement. All these initiatives are expected to yield rich dividends and fructify into financial performance worth showcasing.

Corporate Functions Report

As a responsible and socially conscious institution, J&K Bank is committed to Corporate Social Responsibility (CSR). With an aim to instill a sense of relief and protection among the vulnerable sections of society, the CSR policy of the bank identifies key responsibility areas and seeks to integrate the CSR ideals into its comprehensive mission of empowerment for optimizing its social obligation which focusses on creating sustainable livelihood, promoting education and skill development, promoting environmental sustainability and supporting health and sanitation initiatives.

During the FY 2017-18, the Bank retained its focus on activities aimed at larger community welfare through its CSR initiatives concentrating on marginalized and under-privileged sections of the society to promote inclusive socio-economic wellbeing and growth, empowerment of communities, capacity building & environmental protection.

Major CSR activities in the year 2017-18

Community Development Initiative (Handcarts to street vendors)

In a unique and first of its kind CSR initiative, J&K Bank reached out to marginal section of society engaged in small businesses. In this section, the bank focussed on street vendors like hawkers, cloth merchants & fruit sellers who were provided with branded and designed handcarts to carve out a better financial standing by increasing their sales in an organized manner. Under the initiative, Bank distributed as many as fifty (50) Handcarts fitted with state-of-the-art solar lighting system among the poorest of the poor.

Education

Continuing its innovative CSR initiative of Remote Child Sponsorship Programme (RCSP), the Bank brought socially and financially weak children (mostly orphans) and under-privileged children under its ambit for the sake of seeking primary education through leading concerned non-governmental organization (NGO) CHINAR KASHMIR. For the year, 2017-18, Bank adopted 50 children for the programme.

The Bank also donated two (02) Eco-friendly battery driven vehicles to the University of Kashmir to make the movement of differently-abled students within the campus hassle free. In addition to this, the Bank donated a substantial amount to STUDENTS' WELFARE FUND of the university meant for poor children who find it difficult to get the admission despite being meritorious.

Project MUSKAAN for differently abled

The Bank believes in empowering the marginalized sections of society, hence its concern for such neglected segments comprises of differently abled, orphans and under-privileged children. Under Project "MUSKAAN" Bank has adopted around 200 differently abled children through registered NGOs like Voluntary Medicare Society, Chotey Taarey Foundation, & Bijbehara helpline. The objective of this 'MUSKAAN' initiative vouches the Bank's concern for such children and its step towards elimination of discrimination and empowerment of such sections of society.

Healthcare

Taking holistic approach towards the collective health of people across the state, the Bank unfailingly implements its robust endowment programme. During the year, a good number of patients suffering from Hemophilia & Hepatitis C were provided with lifesaving drugs under Preventive Healthcare programme of the bank. This Preventive Healthcare step remained the focus of Bank's proactive support especially towards the deprived sections of society through a mix of means.

Sanitation

In line with the mission to end open defecation in India by 2019, Swach Bharat Mission has also sought active participation from the corporate sector to tackle the issue. During the year under report, the Bank carried out a massive sanitation programme under "Swachta Hi Seva" where cleanliness drives were carried out in hospitals, public places, schools and district headquarters to impress upon the people how important it is to keep their surroundings neat & clean. At the same time, important machinery like mopping machines were supplied to hospitals & courts to keep such important public places free of dirt.

Upgradation of Old Age Homes/Orphanages

Extending its CSR reach to the remotest part of the Ladakh region, the Bank contributed a substantial amount to an International Old Age Home "Mahabodhi" housing more than 600 people which include elderly citizens, visually impaired children, monks, nuns, volunteers & children from under-privileged families. The contribution was made so that old age people and other distressed lot being rehabilitated at the HOME are benefitted in more than one way. Similarly, two other organizations in Jammu region namely Association for Social Health in India (ASHI) J&K Branch & Samaj Kalyan Kendra, working for the cause of orphans, particularly girls were provided financial assistance to carry on their welfare programmes for the perpetual benefit of such children.

Preserving Ecology/Heritage

Under the "Environmental Excellence Programme" the Bank has been undertaking number of measures like planting