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CREDIT OPINION
28 July 2021

Update

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RATINGS

Zenith Bank Plc

Domicile	Lagos, Nigeria
Long Term CRR	B2
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	B2
Type	Senior Unsecured - Fgn Curr
Outlook	Negative
Long Term Deposit	B2
Type	LT Bank Deposits - Fgn Curr
Outlook	Negative

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Zenith Bank Plc

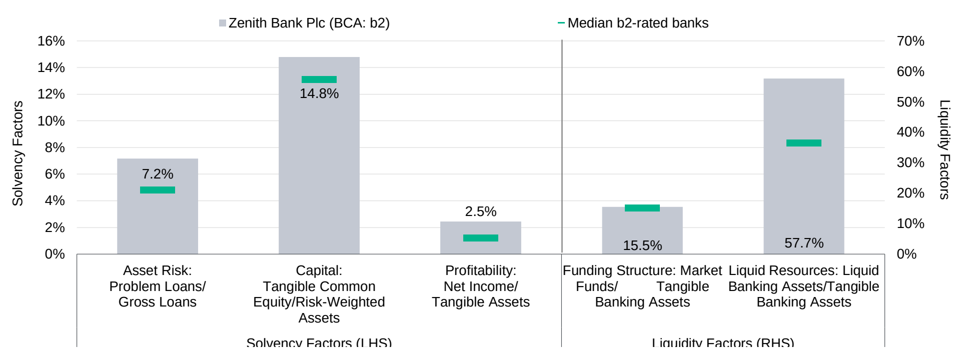
Update post Q1 2020 results

Summary

Zenith Bank Plc's (Zenith) B2 deposit rating is aligned with its b2 Baseline Credit Assessment (BCA), which is at the same level as the rating of the Government of Nigeria (B2 negative).

Zenith's b2 BCA reflects the bank's strong capitalisation buffers, predominantly deposit-funded balance sheet, solid liquidity and strong profitability underpinned by the bank's robust franchise. These strengths are moderated by Nigeria's challenging operating environment, as well as the bank's relatively high problem loans and high reliance on corporate deposits (which tend to be more confidence sensitive than retail deposits).

Exhibit 1
Rating Scorecard - Key financial ratios



The problem loan and profitability ratios are the weaker of the average of three-year ratios and the latest reported quarterly ratios. The capital ratio is the latest reported figure. The funding and liquid assets ratios are the latest year-end figures.
Source: Moody's Investors Service

Credit strengths

» Strong capitalisation buffers

» Strong profitability reflects robust corporate banking franchise underpinned by strong ties with large corporate clients

» Strong liquidity buffers, moderated by tight foreign exchange liquidity in Nigeria

Credit challenges

» Challenging operating environment in Nigeria, combined with the bank's high exposure to foreign-currency loans, pose risks to asset quality

» Sizeable reliance on corporate deposits (albeit gradually declining given growing retail deposit base)

Outlook

The negative outlook reflects the negative outlook the sovereign rating (which signals potential weakening in the Nigerian government's credit strength, to which Nigerian banks are exposed) and the potential weakening in the credit profile of local banks amid a challenging environment.

Factors that could lead to an upgrade

Upwards pressure on the long-term deposit rating of Zenith is limited given the negative outlook.

Factors that could lead to a downgrade

Downwards pressure on the long-term ratings of Zenith could result from a deterioration in the creditworthiness of Nigeria (as would be indicated by a downgrade of the sovereign rating) or a material deterioration in operating environment.

Key indicators

Exhibit 2

Zenith Bank Plc (Consolidated Financials) [1]

	03-21[2]	12-20[2]	12-19[2]	12-18[2]	12-17[2]	CAGR/Avg.[3]
Total Assets (NGN Million)	8,682,815.0	8,481,272.0	6,346,879.0	5,955,710.0	5,595,253.0	14.5[4]
Total Assets (USD Million)	21,203.5	21,485.2	17,488.4	16,384.3	15,542.4	10.0[4]
Tangible Common Equity (NGN Million)	1,032,691.0	1,058,155.0	900,455.0	787,677.0	789,411.0	8.6[4]
Tangible Common Equity (USD Million)	2,521.8	2,680.6	2,481.1	2,166.9	2,192.8	4.4[4]
Problem Loans / Gross Loans (%)	6.4	6.4	6.8	9.0	4.7	6.7[5]
Tangible Common Equity / Risk Weighted Assets (%)	--	14.8	17.7	18.9	20.5	18.0[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	16.3	15.6	15.9	18.5	11.2	15.5[5]
Net Interest Margin (%)	4.0	4.1	4.6	5.3	5.2	4.6[5]
PPI / Average RWA (%)	--	4.8	6.0	6.2	7.6	6.1[6]
Net Income / Tangible Assets (%)	2.4	2.7	3.3	3.3	3.1	3.0[5]
Cost / Income Ratio (%)	51.7	46.4	46.4	47.4	42.9	47.0[5]
Market Funds / Tangible Banking Assets (%)	12.9	15.5	12.2	20.4	19.6	16.1[5]
Liquid Banking Assets / Tangible Banking Assets (%)	46.0	57.7	50.1	45.1	43.6	48.5[5]
Gross Loans / Due to Customers (%)	52.6	54.7	57.8	54.6	65.5	57.0[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel II; IFRS. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel II periods.
Sources: Moody's Investors Service and company filings

Profile

Zenith Bank Plc (Zenith) is a full-service commercial bank that offers corporate banking, commercial and consumer banking, personal and private banking, trade and foreign-exchange, and treasury and cash management services. The bank was established in May 1990 and commenced operations in July of the same year as a commercial bank. Zenith became a public limited company on June 17, 2004, and was listed on the Nigerian Stock Exchange (NSE) on October 21, 2004.

As of March 2021, Zenith reported consolidated total assets of NGN8.7 trillion (about $21.2 billion).

Detailed credit considerations

Challenging operating environment in Nigeria, combined with the bank's high exposure to foreign-currency loans, pose risks to asset quality

We expect Zenith's asset quality to face pressure from the weak operating environment in Nigeria and the future phase our of support measures, which will lead to problem loans formation. However, we expect future asset quality pressure for Zenith to be lower than that of its Nigerian peers given the bank's robust risk management framework.

Zenith has a high exposure to foreign-currency loans which, similar to other Nigerian banks, poses some asset risk. The bank's proportion of foreign currency loans denominated in US dollars stood at 44% of total loans as of December 2020 (39% in 2019 and 46% in 2018). Foreign-currency loans pose a risk because significant depreciation of the local currency would weaken the repayment capacity of the portion of borrowers that predominantly earn revenue in the local currency.

Similar to other Nigerian banks, Zenith's relatively high stock of restructured loans poses some risk to asset quality. The bank's restructured loans increased to 22% of gross loans in 2020, from 18% in 2019 and 15% in 2018. Restructured loans primarily included exposures to the oil and gas sector (72% of the stock) and to the public sector (19%). The balance of loans and advances that are not impaired but exhibit a significant increase in credit risk — classified in the Stage 2 bucket under IFRS9 — increased to a high 19.8% of gross loans as of December 2020 from 7.3% as of December 2019.

Rapid growth, again similar to local peers, also poses some risk since it increases the unseasoned portion of the loan book in a challenging environment. Zenith's gross loans increased by 19% in 2020. However, the credit growth is lower when adjusted for the inflation rate of 16% in 2020.

We expect that Zenith's prudent risk management will help limit the extent of asset quality deterioration in comparison to local peers. In addition, the bank's exposure to resilient large corporates, combined with its relatively diversified loan book (in comparison to local peers), will also support asset quality.

The bank's problem loans[1] to gross loans ratio decreased slightly to 6.4% as of December 2020 (6.4% as of March 2021) from 6.8% as of December 2019. The bank's problem loan coverage provides some buffer, with loan loss reserves representing 75% of problem loans as of March 2021.

Strong capitalisation buffer

We expect the bank's capitalisation to remain strong over the next 12-18 months, reflecting resilient profitability and prudent dividend policy. Nonetheless, we expect the capitalisation to decline modestly in line with rapid growth and provisioning needs.

As of December 2020, the bank's tangible common equity to risk-weighted assets (TCE ratio) declined noticeably to 14.8% from 17.7% as of December 2019, mainly due to growth in rapid asset growth. We adjust the bank’s TCE ratio for the risk weighting on the bank’s holding of Nigerian government securities, in line with the Basel II framework. As of December 2020, Zenith's reported Tier 1 ratio was 21.3% and its reoprted capital adequacy ratio was 23.1%.

However, potential local currency volatility will continue to poses some risk to the bank's capitalisation. Given Zenith's sizeable exposure to foreign currency loans, a depreciation of the local currency would increase the bank's risk weighted assets and potentially reduce the capital ratios.

Strong profitability reflects robust corporate banking franchise underpinned by strong ties with large corporate clients

A key credit strength is Zenith's robust profitability, which reflects its strong domestic corporate banking franchise.

The bank's net interest margins were high at 4.1% during the year 2020 (4.0% during the first three months of 2021), primarily reflecting Zenith corporate gathering franchise allowing it to attract cheaper deposits than its local peers. Zenith's non-interest income increased by 9% during 2020 (supported by trading income and other operating income), and the contribution of non-interest income to total revenues increased to 40% in 2020 from 37% in 2019.

The bank's cost-to-income ratio stood at 52% during the first three months of 2021. We expect Zenith' cost of risk to remain elevated in 2021, reflecting the lagged impact of the pandemic on borrowers. The bank's cost of risk, computed as loan loss provisions divided by gross loans, was around 1.3% in 2020.

Solid funding and liquidity, moderated by tight foreign-exchange liquidity in Nigeria

Zenith is predominantly deposit funded, with a low reliance on more sensitive market funds. Deposits made up about 75% of the bank's funding sources as of March 2021. The bank's market funding ratio decreased slightly to 12.9% as of March 2021 from 15.5% at year-end 2020.

Zenith's high level of non-retail deposits, at 68% of total deposit poses some risk since corporate deposits tend to be more confidence sensitive than retail deposits. However, we expect the bank to continue to increase increased its retail deposit base, which materially grew to 32% of total deposits in December 2020 from 26.0% in December 2019.

Zenith's liquidity is strong, with liquid banking assets-to-tangible banking assets at 46% as of March 2021. The bank also has robust foreign-currency liquidity, with dollar liquid assets-to-total dollar funding (deposits + borrowings) of 82% as of March 2021. However, we continue to expect a tight foreign-currency liquidity environment in Nigeria this year, albeit slightly improved from 2020.

Environmental, social and governance considerations

In line with our general view for the banking sector, Zenith has low exposure to environmental risks. However, Zenith's material exposure to the oil and gas industry is an environmental risk that requires monitoring, particularly as the transition to a low carbon economy accelerates. See our Environmental risk heat map for further information.

We consider banks to face moderate Social risks (see social risk heatmaps). The most relevant social risks for banks arise from the way they interact with their customers. Social risks are particularly high in the area of data security and customer privacy, which is partly mitigated by sizeable technology investments and banks' long track record of handling sensitive client data. Fines and reputational damage because of product mis-selling or other types of misconduct is a further social risk. Societal trends are also relevant in a number of areas, such as shifting customer preferences towards digital banking services increasing information technology cost or socially driven policy agendas that may translate into regulations that affect banks' revenue base. We also regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety.

Governance is highly relevant for Zenith. Corporate governance weaknesses can lead to a deterioration in a company's credit quality, while governance strengths can benefit its credit profile. Governance risks are largely internal rather than externally driven, and for Zenith, we do not highlight any particular governance issues, given its appropriate risk management framework. Nonetheless, corporate governance remains a key credit consideration and requires ongoing monitoring.

Support and structural considerations

Government support

Given that Zenith's BCA is at the same level as the Nigerian government's issuer rating of B2, negative, we do not incorporate any rating uplift on the bank's BCA despite our assessment of a High probability of support in case of financial stress, given the strong market position of the bank (second-largest bank in Nigeria, with a market share of 18.1% of total assets and its designation as a systemically important bank).

Counterparty Risk Ratings (CRRs)

CRRs are opinions of the ability of entities to honour the uncollateralised portion of non-debt counterparty financial liabilities (CRR liabilities) and also reflect the expected financial losses in the event such liabilities are not honoured. CRR liabilities typically relate to transactions with unrelated parties. Examples of CRR liabilities include the uncollateralised portion of payables arising from derivatives transactions and the uncollateralised portion of liabilities under sale and repurchase agreements. CRRs are not applicable to funding commitments or other obligations associated with covered bonds, letters of credit, guarantees, servicer and trustee obligations, and other similar obligations that arise from a bank performing its essential operating functions.

Zenith's local currency CRRs is positioned at B1/Not Prime and the foreign currency CRR is positioned at B2/Not Prime as it is constrained by the foreign currency country ceiling.

The CRRs are positioned one notch above the Adjusted BCA of b2, and therefore above the deposit ratings, reflecting our view that its probability of default is lower than that of deposits.

Counterparty Risk (CR) Assessment

CR Assessments are opinions of how counterparty obligations are likely to be treated if a bank fails and are distinct from debt and deposit ratings in that they consider only the risk of default rather than the likelihood of default and the expected financial loss suffered in the event of default, and apply to counterparty obligations and contractual commitments rather than debt or deposit instruments. The CR assessment is an opinion of the counterparty risk related to a bank's covered bonds, contractual performance obligations (servicing), derivatives (for example, swaps), letters of credit, guarantees and liquidity facilities.

Zenith's CR Assessment is positioned at B2(cr)/Not Prime(cr)

The CR Assessment is positioned one notch above the Adjusted BCA of b2, and therefore above the deposit ratings, reflecting our view that its probability of default is lower than that of deposits. We believe senior obligations represented by the CR Assessment will be more likely preserved to limit contagion, minimise losses and avoid disruption of critical functions.

National scale rating (NSR)

Zenith's NSRs of Aa3.ng/NG-1 for local and foreign currency deposits are generated from the bank's global scale ratings through maps specific to each country. NSRs are not intended to rank credits across multiple countries; instead they provide a measure of relative creditworthiness within a single country (Nigeria in the case of Zenith). Our NSRs are given a two-letter suffix to distinguish them from our global scale ratings. For example, NSRs in Nigeria have the country abbreviation “ng.”

Zenith's NSRs capture the bank's robust capital buffers, which provide a relatively thick buffer to withstand asset-quality deterioration; its high liquidity buffers, complimenting a predominantly deposit-funded balance sheet; and a strong and well-established franchise, which allows the bank to attract inexpensive deposits and to lend to high-credit-quality borrowers (relative to other Nigerian banks). These strengths are partially moderated by the bank's high proportion of more confidence-sensitive corporate deposits versus retail deposits.

Rating methodology and scorecard factors

Exhibit 3
Zenith Bank Plc

Macro Factors		
Weighted Macro Profile	**Very Weak +**	**100%**

Factor	Historic Ratio	Initial Score	Expected Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	7.2%	caa1	↔	caa2	Expected trend	
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel II)	14.8%	b2	↑	b1	Expected trend	
Profitability						
Net Income / Tangible Assets	2.4%	ba3	↔	ba3	Expected trend	
Combined Solvency Score		b2		b2		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	15.5%	b3	↔	b2	Deposit quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	57.7%	ba3	↔	b2	Quality of liquid assets	
Combined Liquidity Score		b2		b2		
Financial Profile				b2		
Qualitative Adjustments				Adjustment		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint				B2		
BCA Scorecard-indicated Outcome - Range				b1 - b3		
Assigned BCA				b2		
Affiliate Support notching				0		
Adjusted BCA				b2		

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	1	0	b1	0	B1	B2
Counterparty Risk Assessment	1	0	b1 (cr)	0	B1(cr)	
Deposits	0	0	b2	0	B2	B2
Senior unsecured bank debt	0	0	b2	0	B2	B2

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.
Source: Moody's Investors Service

Ratings

Exhibit 4

Category	Moody's Rating
ZENITH BANK PLC	
Outlook	Negative
Counterparty Risk Rating -Fgn Curr	B2/NP
Counterparty Risk Rating -Dom Curr	B1/NP
Bank Deposits	B2/NP
Baseline Credit Assessment	b2
Adjusted Baseline Credit Assessment	b2
Counterparty Risk Assessment	B1(cr)/NP(cr)
Issuer Rating	B2
Senior Unsecured	B2
ST Issuer Rating	NP

Source: Moody's Investors Service

Endnotes

1 Problem loans include the total stock of loans classified under the Stage 3 bucket as per IFRS9 accounting standards

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