MOODY'S
INVESTORS SERVICE

CREDIT OPINION

20 November 2017

Update

Rate this Research

RATINGS

Zenith Bank Plc

Domicile	Lagos, Nigeria
Long Term Debt	B2
Type	Senior Unsecured - Fgn Curr
Outlook	Stable
Long Term Deposit	B3
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

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

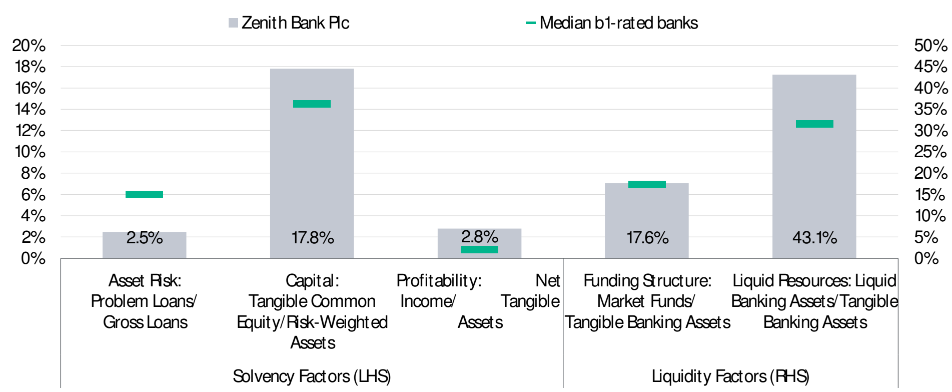
Update following rating action

Summary

On 10 November 2017, we downgraded Zenith Bank Plc's (Zenith) baseline credit assessment (BCA) to b2 from b1, long-term local currency deposit rating to B2 from B1, long term foreign currency deposit rating to B3 from B2, long-term local and foreign currency issuer ratings to B2 from B1, long term local currency national scale deposit ratings to Aa3.ng from Aaa.ng, foreign currency national scale deposit ratings to A3.ng/NG-2 from Aa3.ng/NG-1, long-term CR Assessment to B1(cr) from Ba3(cr). The downgrades are primarily driven by the bank's high exposure to government securities that links the bank's credit profile to that of the government. The decision to downgrade the long term foreign currency deposit rating to B3 and the foreign currency national scale ratings to A3.ng/NG-2, follows the downgrade of the relevant country ceiling, which captures foreign currency and convertibility risks.

Zenith Bank's BCA of b2 reflects (1) the bank's resilient earnings generating capacity and robust capital buffers, which together provide a cushion to withstand asset quality deterioration; (2) the bank's high liquidity buffers and a predominantly deposit funded balance sheet; and (3) the bank's robust franchise, which allows it to attract inexpensive deposits and to lend to high credit quality borrowers (relative to other Nigerian banks), resulting in relatively strong asset quality metrics and low credit costs. These strengths are balanced against (4) Nigeria's challenging operating environment which will negatively affect the bank's asset quality and revenue growth; and (5) the bank's high proportion of more confidence sensitive corporate deposits versus retail deposits.

Exhibit 1
Rating Scorecard
Key Financial Ratios



Source: Moody's Investors Service

Credit strengths

» Relatively strong asset quality with a problem loans ratio that is superior to b2-rated peers

» Strong franchise which supports revenue generation and profitability, in turn supporting capital

» Predominantly deposit funded and relatively strong liquidity buffers

Credit challenges

» Nigeria's challenging macroeconomic environment

» Relatively higher dependence on confidence sensitive corporate deposits over retail deposits

Rating outlook

All ratings assigned to Zenith carry a stable outlook. The stable outlook reflects our expectations that the bank's pre-provision profits can absorb any increase in loan loss provisions and that overall, the bank's credit fundamentals will continue to compare favourably with peers despite continued pressures arising from the challenging operating environment in Nigeria.

Factors that could lead to an upgrade

Given that Zenith's BCA is already at the same level as Nigeria's issuer rating of B1, there is limited scope for an upgrade in the short term. Zenith's ratings could be upgraded if operating conditions improve and Nigeria's sovereign rating is upgraded, while the bank maintains its strong financial metrics.

Factors that could lead to a downgrade

Zenith's ratings could be downgraded if its asset quality deteriorates meaningfully, putting pressure on the bank's profitability and capital buffers. A substantial deterioration of the bank's foreign currency liquidity buffers would also likely trigger a downgrade, as would a downgrade of the sovereign itself.

Key indicators

Exhibit 2

Zenith Bank Plc (Consolidated Financials) [1]

	9-17[2]	12-16[2]	12-15[2]	12-14[2]	12-13[3]	CAGR/Avg.[4]
Total Assets (NGN million)	5,131,818	4,739,825	4,006,842	3,755,264	3,143,133	14.0[5]
Total Assets (USD million)	14,295	15,048	20,130	20,521	19,651	-8.1[5]
Tangible Common Equity (NGN million)	745,665	687,887	586,206	543,818	497,830	11.4[5]
Tangible Common Equity (USD million)	2,077	2,184	2,945	2,972	3,112	-10.2[5]
Problem Loans / Gross Loans (%)	-	2.5	1.2	0.7	1.1	1.4[6]
Tangible Common Equity / Risk Weighted Assets (%)	-	17.8	17.9	17.4	19.6	17.7[7]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	-	7.7	4.0	2.1	2.6	4.1[6]
Net Interest Margin (%)	5.6	5.6	5.9	6.4	7.2	6.1[6]
PPI / Average RWA (%)	-	5.2	4.7	4.2	4.9	4.7[7]
Net Income / Tangible Assets (%)	3.4	2.7	2.6	2.6	3.0	2.9[6]
Cost / Income Ratio (%)	46.2	48.0	51.2	55.3	55.7	51.3[6]
Market Funds / Tangible Banking Assets (%)	21.2	17.6	16.1	9.7	5.9	14.1[6]
Liquid Banking Assets / Tangible Banking Assets (%)	48.4	43.1	42.3	45.8	46.5	45.2[6]
Gross Loans / Due to Customers (%)	74.2	79.1	79.5	69.3	57.7	72.0[6]

[1] All figures and ratios are adjusted using Moody's standard adjustments [2] Basel II; IFRS [3] Basel I; IFRS [4] May include rounding differences due to scale of reported amounts [5] Compound Annual Growth Rate (%) based on time period presented for the latest accounting regime [6] Simple average of periods presented for the latest accounting regime. [7] Simple average of Basel II periods presented

Source: Moody's Financial Metrics

Profile

Zenith Bank Plc (Zenith) is a full-service commercial bank that offers corporate banking, commercial and consumer banking, personal and private banking, trade service and foreign exchange and treasury and cash management services. It 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 following a highly successful Initial Public Offering (IPO).

As of June 2017, Zenith reported consolidated total assets of NGN4.3 trillion (about $13.8 billion).

Detailed credit considerations

Nigeria macro profile: Very Weak+

Our methodology comprises an assessment of a bank's operating environment which, for Zenith, is based on our assessment of Nigeria's macro profile, where the bank conducts most of its business.

We assign a 'Very Weak +' macro profile score to Nigeria, reflecting the country's fiscal and economic dependence on the oil and gas sector and its high dollarization, which pose asset quality volatility and foreign currency liquidity challenges, as well as Nigeria's evolving institutions and relatively high level of corruption (based on indices from the World Bank).

While the banks' operating environment is difficult, the Nigerian financial system has also shown strong resilience to shocks and it presents sizable growth opportunities given low banking penetration, especially in the profitable retail and SME space, which will allow the banking sector to expand steadily.

Strong asset quality metrics underpinned by a conservative approach to risk

A key strength of Zenith Bank's credit profile is its consistently low level of adjusted NPLs. Zenith's adjusted NPL ratio of 3.5% as of June 2017 compares favorably with peers internationally (Moody's adjusted NPL ratio is defined as individually impaired loans plus loans that are overdue by more than 90 days, but not impaired, as a percentage of gross loans). Zenith also reported a solid NPL coverage ratio of 117% (including regulatory reserves), which compares positively against b2 rated banks.

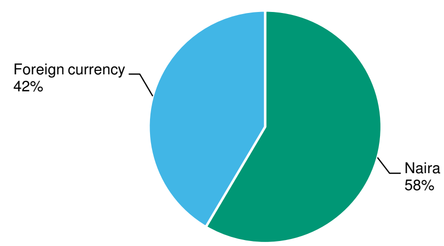
The bank's low NPLs are on account of its exposure to debtors with relatively stronger credit profiles, such as large and diversified Nigerian conglomerates. The bank also adopts a prudent approach to risk management which includes conservative underwriting standards and the use of robust internal procedures. The bank's conservative stance was demonstrated in the last crisis (2009) when reported NPLs peaked at just 6.5%, compared to around 37% for the banking system.

However, some aspects of the bank's current loan portfolio are credit negative, in our view. Though lower than the banking system average of greater than 45%, we view the bank's exposure to foreign currency denominated loans (42% of total loans as of June 2017) as a weakness (see Exhibit 3). The foreign currency denominated portfolio exposes the bank's borrowers to the exchange rate volatility of the Naira, though we note that the bank has restructured many of these loans and, as such, they remain performing. Additionally, Zenith Bank's loan portfolio is concentrated; single name concentration risk is indicated by the bank's top 20 borrowers, which make up over 90% of the bank's tangible capital, exposing capital to significant erosions if one or a few of the top obligors default. It should be noted, however, that Zenith's level of concentration risk is significantly less than that witnessed in other Nigerian banks.

Exhibit 3

Zenith foreign currency loans exposure is high at 42% of total loans

Loans and Advances Currency Exposures as of June 2017



Source: Banks financials statements and presentations; Moody's Investors Service

Solid capital buffers reinforced by a robust franchise which supports profitability

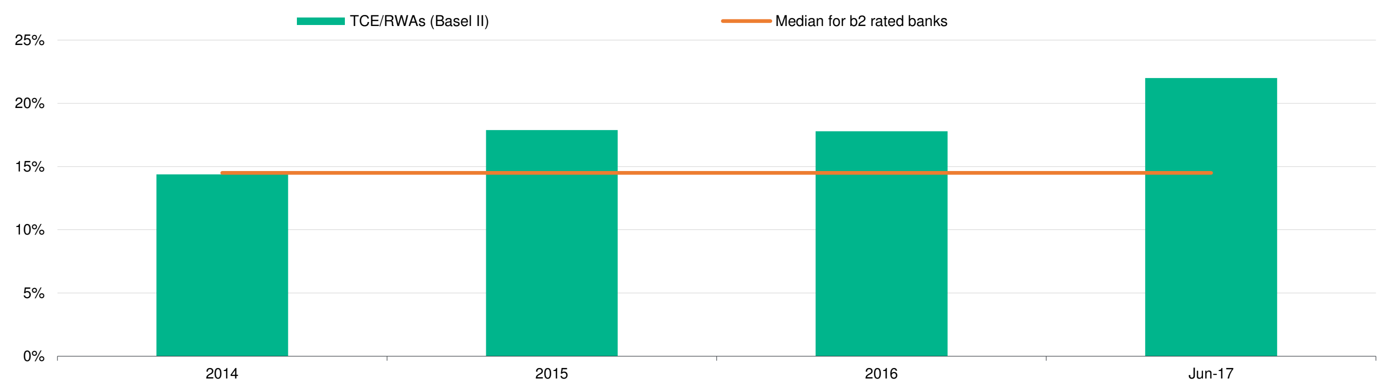
Zenith Bank's credit profile is also underpinned by robust capital buffers. As of December 2016 tangible common equity as a percentage of risk-weighted assets stood at 23%. Zenith's ratio is significantly higher than the global b2 BCA peer median of 14.5%.

Going forward, we expect the bank's capitalisation to remain strong, primarily because of Zenith's resilient profitability metrics. Zenith's net income to tangible assets has remained fairly stable over the last year and was 3.1% as of June 2017, significantly better than the global b2 BCA peer median of 0.8%. Profitability is supported by the bank's robust franchise which allows it to attract cheaper deposits and lend to high credit quality borrowers (relative to other Nigerian banks), resulting in relatively low credit costs.

Exhibit 4

Zenith holds thicker capital buffers compared to global peers

Tangible Common Equity As a Percent of Risk Weighted Assets



Source: Moody's Investors Service

That said, we view Zenith's reported capitalization as being moderated by the bank's exposure to foreign currency loans and to the government of Nigeria. Government securities are risk-weighted at zero under the domestic regulatory framework, as such, in order to more fully capture the risks associated with government bonds, our practice globally is to assign a risk-weight to sovereign debt holdings, as per the Basel Committee. For a sovereign rated B2, we assign a 100% risk-weighting to government securities. Regarding the bank's exposure to foreign currency loans, the bank's capital is vulnerable to a further depreciation of the Naira against foreign currencies, especially dollars, as a Naira depreciation will inflate risk-weighted assets.

However, our scenario analysis shows that the bank's capital levels remain robust even under a stressed scenario given the bank's high capital buffers.

Low reliance on market funding and high liquidity buffers moderated by predominantly corporates deposits

Our BCA also reflects the bank's solid liability profile. The bank is predominantly deposit funded with a low reliance on more sensitive market funds (deposits make up about 74% of the bank's funding sources). However, we note that the majority of deposits are corporate deposits (about 56%) which we consider to be more market sensitive and expensive than retail deposits.

Given the tight dollar liquidity environment on account of lower oil prices and the introduction of the Treasury Single Account (which requires federal government agencies to keep their excess earnings in a single account maintained with the Central Bank of Nigeria) Zenith Bank's foreign currency deposits fell by around 9% in 2016, adjusting out the effect of Naira depreciation. However, this decline did not pose significant risks for the bank given the bank's significant stock of high quality liquid assets in dollars.

Overall, the bank continues to maintain a high liquidity ratio which provides a thick cushion, with a liquidity ratio of 61% against a regulatory requirement of 30% as of June 2017. The bank's dollar liquid assets to total dollar deposits was also strong at 24% as of June 2017.

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, stable, we do not incorporate any rating uplift on the bank's BCA despite Moody's assessment of a 'High' probability of support in case of financial stress, given the strong market position of the bank (2nd largest bank in Nigeria with a market share of 15% of total assets and designated a 'Systemically Important Bank').

We assign to Zenith Foreign Currency Deposit Ratings of B2/Not Prime, which is constrained at a lower level due to the convertibility risks associated with foreign currency.

Counterparty risk assessment

Zenith's CR Assessment is positioned at B1(cr)/ Not-Prime(cr). The CR Assessment is positioned one notch above the Adjusted long-term local currency deposit rating of B2, 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 in order to limit contagion, minimize losses and avoid disruption of critical functions.

National scale rating

Zenith's national scale ratings of Aa3.ng/NG-1 for local currency deposits and A3.ng/NG-2 for 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). Moody's NSRs are given a two-letter suffix to distinguish them from the agency's Global Scale Ratings. For example, NSRs in Nigeria have the country abbreviation "ng".

Zenith's national scale ratings capture the bank's (1) robust capital buffers, which provide a relatively thick cushion to withstand asset quality deterioration; (2) low stock of reported NPLs, accounting for around 3% of gross loans against a system average of around 14%); (3) high liquidity buffers, complimenting a predominantly deposit funded balance sheet; and (4) 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), resulting in relatively low NPLs and credit costs. 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 5

Zenith Bank Plc

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

Factor	**Historic Ratio**	**Macro Adjusted Score**	**Credit Trend**	**Assigned Score**	**Key driver #1**	**Key driver #2**
Solvency						
Asset Risk						
Problem Loans / Gross Loans	2.5%	b2	←→	b3		
Capital						
TCE / RWA	17.8%	ba3	←→	b1	Expected trend	
Profitability						
Net Income / Tangible Assets	2.8%	ba1	←→	ba2	Expected trend	
Combined Solvency Score		ba3		b1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	17.6%	b3	←→	b2	Deposit quality	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	43.1%	b1	←→	b1		
Combined Liquidity Score		b2		b2		
Financial Profile				b1		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint:				--		
Scorecard Calculated BCA range				--		
Assigned BCA				--		
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 Assessment	1	0	b1 (cr)	--	B1 (cr)	--
Deposits	0	0	b2	--	B2	B3
Senior unsecured bank debt	0	0	b2	--	B2	B2

Source: Moody's Financial Metrics

Ratings

Exhibit 6

Category	Moody's Rating
ZENITH BANK PLC	
Outlook	Stable
Bank Deposits -Fgn Curr	B3/NP
Bank Deposits -Dom Curr	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

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