

Zenith Bank Plc. (ZENITH.NL)

Initial View

| | |
|----------------------------------|-----------------|
| Price | ₦31.00 |
| FVE (<i>last communicated</i>) | ₦36.27 |
| 52-week range | ₦29.40 – ₦33.51 |
| Market Cap. (₦'mn) | 973,291 |
| 1-month Avg. Vol | 22,224,830 |
| Curr. PE | 5.47x |

ZENITH:NL - Share Price Trend



Analyst(s)

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A Chicken and Egg Situation

- Full-year 2017 result of Zenith Bank (Zenith) showed EPS growth of 37.2% YoY to ₦5.67 (2016: ₦4.13) largely on the back of strong growth in non-interest revenue (+119.2% YoY to ₦270 billion) which masked elevated loan loss provision (+203.6% YoY to ₦98.3 billion). The bank declared a final dividend of ₦2.45, which alongside interim dividend of ₦0.25 translates to total dividend of ₦2.70. At current pricing, final dividend translates to a yield of 8%.
- Possible haircut on 9mobile exposure?** Over Q4 2017, Zenith booked ~₦52 billion in impairment (9M 17: ₦47 billion) with Cost of Risk expanding by 8.8pps QoQ to 9.7%. In ascertaining the driver for the higher impairment, breakdowns provided by Zenith throws up higher impairment (specific) to ICT and Oil & Gas sectors over H2 2017 by 1724% and 233.8% accordingly. While we await management clarification on the assets in both sectors, our findings suggest that the sale of 9mobile resulted in a discount to market value. Consequently, in line with IFRS, the bank must have taken a haircut of ~40% on its exposure to the telecoms firm. Non-performing loans (NPL) printed at 4.7% (+50bps QoQ) with Oil & Gas, General Commerce and Transport contributing ~37%, 28% and 16% in that order.

- ***Non-interest Revenue boosted by trading income.*** As earlier stated, the key driver for the earnings growth, despite higher impairment, was the non-interest revenue (NIR) which expanded over two-fold YoY. Over the Q4 2017, NIR expanded 97% QoQ with much of the jump growth in earnings emanating from trading income (+362% QoQ). First off, the bank reported treasury bills income of ₦36 billion like prior quarter (₦34 billion) which reflects trading income from its swap position (Notional value: \$1.5 billion). Irrespective, much of the improvement in NIR stemmed from FX trading income of ₦39 billion (Q3 17: FX trading loss of ₦17.6 billion).
- ***\$250 million net-long position drives FCY gains.*** Further supporting the jump in NIR was the ₦5.5 billion booked in the quarter, stemming from FCY revaluation gains on its net FCY position which our estimate puts at \$250 million. The gains reflected revaluation of its FCY position at the NIFEX rate (₦330/\$) from prior CBN rate (₦305/\$).
- ***Eurobond coupon payment weakens funding cost.*** Despite a 13% expansion in interest income with asset yields rising 35bps QoQ to 8.5% (stemming from interbank placement and loans), Zenith funding cost worsened over Q4. Interest expense jumped sharply by 52% QoQ with cost of funds (WACF) expanding by 142bps QoQ to 5.0%. Looking through the breakdowns, funding cost pressure emanated from interest expense on borrowed funds which jumped 230% QoQ to ₦47 billion. From our analysis, the jump in interest expense on borrowed funds emanated from coupon payment on its \$500 million Eurobond issued in May 2017 and first coupon payment due in November 2017. Consequently, Net Interest Margin (NIM) contracted by 100bps QoQ to 5.0%. Overall, despite higher NIR, the impact of decline in net interest income (-9.6% QoQ) and higher impairment (+999% QoQ) dipped EPS in Q4 by 9.7% QoQ to ₦1.55 (Q3 17: ₦1.72).
- The Bank will be holding a conference call Tomorrow, Wednesday March 14 at 2pm Lagos Time (1pm London/ 3pm Johannesburg/ 9am New York). Click [here](#) for conference call details.
- Zenith is trading at a P/B of 1.19x which is at a discount to peers of 1.7x - ROE of 21.7%. Our last communicated FVE on Zenith Bank is ₦36.37 which translates to an **OVERWEIGHT** rating on the stock. We will revisit our numbers after further analysis and discussion with management.

Summary of Results and Forecast

| N'million | FY 2017 | FY 2017E | FY 2016 | YoY | Q4 2017 | Q3 2017 | QoQ |
|-----------------------------|----------------|----------------|----------------|---------------|----------------|----------------|--------------|
| Gross Earnings | 587,215 | 652,666 | 507,997 | 15.6% | 137,758 | 134,335 | 2.5% |
| Net Interest Income | 257,991 | 265,288 | 240,179 | 7.4% | 56,499 | 62,530 | -9.6% |
| Non-Interest Revenue | 270,561 | 189,048 | 123,440 | 119.2% | 101,084 | 51,294 | 97.1% |
| Operating Expenses | (226,864) | (194,054) | (174,521) | 30.0% | (55,500) | (48,800) | 13.7% |
| Impairment | (98,227) | (51,334) | (32,350) | 203.6% | (51,174) | (4,655) | 999.3% |
| PBT | 203,461 | 208,948 | 156,748 | 29.8% | 50,909 | 60,369 | -15.7% |
| PAT | 177,933 | 177,606 | 129,652 | 37.2% | 48,698 | 53,918 | -9.7% |
| EPS | 5.67 | 5.66 | 4.13 | | 1.55 | 1.72 | |
| DPS | 2.70 | 2.55 | 2.02 | | | | |
| N'million | FY 2017 | FY 2017E | FY 2016 | YoY | | | |
| Loans | 2,100,362 | 2,231,909 | 2,289,365 | -8.3% | | | |
| Total Assets | 5,593,253 | 4,981,324 | 4,739,825 | 18.0% | | | |
| Deposits | 3,437,915 | 3,073,717 | 2,983,621 | 15.2% | | | |
| Total Liabilities | 4,773,595 | 4,179,162 | 4,035,360 | 18.3% | | | |
| Net Assets | 819,658 | 802,162 | 704,465 | 16.4% | | | |
| BVPS | 26.11 | 25.55 | 22.44 | 16.4% | | | |
| | FY 2017 | FY 2016 | YoY (pps) | Q4 2017 | Q3 2017 | YoY (pps) | |
| Assets Yields | 9.7% | 9.2% | 0.5 | 8.5% | 8.2% | 0.3 | |
| WACF | 5.2% | 4.2% | 1.1 | 5.0% | 3.6% | 1.4 | |
| Net Interest Margin | 5.3% | 5.7% | (0.5) | 5.0% | 6.0% | (1.0) | |
| Cost-Income Ratio | 42.9% | 48.0% | (5.1) | 35.2% | 42.9% | (7.7) | |
| Cost of Risk | 4.7% | 1.4% | 3.3 | 9.7% | 0.9% | 8.9 | |
| ROE | 21.7% | 18.4% | 3.3 | 23.8% | 31.9% | (8.2) | |
| CAR | 27.0% | 23.0% | 4.0 | | | | |

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