



Initial View

9 months ended 30<sup>th</sup> September, 2014**Recommendation: STRONG BUY (₦28.7)**

- Zenith Bank Plc (Zenith) reported 12% YoY (6M 14: +13%) rise in gross earnings to ₦273.4 billion for the 9 months ended September 2014. PBT was 8% higher YoY (6M 14: +3%) at ₦86.8 billion while PAT was 5% higher YoY (6M 14: +5%) at ₦71 billion.

***NIR pegs back topline***

- Q3 14 interest income of ₦73.5 billion was mildly lower QoQ but matched our estimates with asset yield and earning asset volumes coming in line with projections. In a repeating dynamic thus far amongst banks that have released Q3 14 results, Zenith's asset growth was primarily driven by loans (+10% to ₦1.5 trillion) and securities (T-bills: +33%, HTM portfolio: +8%). However, non-interest revenue (NIR) disappointed, coming in 30% lower QoQ at ₦15.5 billion, 23% behind estimates. Both fee (-25%) and trading (-39%) income were significantly lower QoQ and the weakness in NIR as a whole was primarily responsible for gross earnings falling 5% short of estimates.

**Income Statement Data**

	2014 – 9M'm	2013 – 9M'm	%chg
Gross Earnings	273,414	243,623	12%
PBT	86,818	80,702	8%
TAX	(15,772)	(12,815)	23%
PAT	71,046	67,887	5%

**Balance Sheet Data**

	2014-Sept 'm	2013 -Dec 'm	%chg
Cash	1,001,815	1,190,292	-16%
Loans	1,526,109	1,251,355	22%
Deposit	2,309,614	2,276,755	1%
Fixed Asset	70,951	69,410	2%
Net Assets	523,932	509,251	3%

**Stock Data**

Price	₦22.75
52 week range	₦19.50 – ₦27.40
Market Cap. (N'm)	714,270.23
1-month Avg. Vol	22,583,006
Curr. PE	7.5x
Bloomberg Ticker	ZENITHBA: NL
Reuters Ticker	ZENITHB.LG

**Zenith Bank Plc- Share Price Trend****Analyst(s)**

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### ***Cost improvements prevent damage to profits***

- On a positive note, despite a 3% QoQ rise in funding base, interest expense contracted 9% QoQ to ₦20.9 billion, 5% ahead of our estimate. The disparate movement indicates an extension of the 2014 focus on cheaper funding with sequential quarterly step-downs in interest expense putting annualized WACF of 3.6% as at 9M 14, 90bps below year-start (-30bps QoQ).
- Opex came in flat for the second quarter running at ₦37.2 billion, 8% below our expectations which had anticipated increase in regulatory costs. This appeared to pan out as other opex increased 5% QoQ but that was offset by an 8% decline in personnel expenses. Annualised cost-to-income ratio dropped 20bps from 6M 14 to 55.2%.
- Impairment charges however doubled QoQ to ₦2 billion which we consider likely related to the wave of asset creation thus far in 2014. Nonetheless, absolute amount remains negligible with cost of risk unchanged from 6M at 0.3%, half our FY 14 estimate.
- Lower interest expense, in particular, helped offset revenue pressures and maintained Q3 14 PAT at ₦29 billion, flat QoQ and matching our estimates. PAT of ₦23.6billion was also flat QoQ but with tax charge 22% above our forecast was 6% behind our estimates. Corresponding PBT margin of 32% is 100bps higher than 6M 14 but lower by that same margin YoY while PAT margin of 26% is flat from 6M 14 but 200bps behind YoY.

### ***Price declines restore BUY recommendation***

- Zenith's ability to sustain operating performance despite industry pressures remains a key positive in our view. Having closely tracked expectations for operating performance thus far, we envisage moderate revisions to our model. Perhaps more pertinently, pressures on market price, alongside the broader market, make Zenith's valuation much more compelling than at our last review. Whilst current P.E of 7.5x (prev. 8.3x) and P/B of 1.4x (prev 1.6x) remain at premia to peers' 6x and 1x respectively, justifiably so in our view. The expanded upside to our current **(FVE: ₦28.7)** prompts us to a one-notch rating upgrade to **STRONG BUY**.
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## Summary of forecasts

Quarterly Forecasts	Q4 2014E	Q1 2015E	Q2 2015E	Q3 2015E	
Net interest income	52,024	52,485	53,579	54,672	
Non-interest income	17,023	22,653	23,125	23,597	
<b>Total Revenue</b>	<b>69,047</b>	<b>75,139</b>	<b>76,704</b>	<b>78,269</b>	
Total Operating Costs	(37,655)	(40,353)	(41,194)	(42,035)	
<b>Operating Profit</b>	<b>31,391</b>	<b>34,785</b>	<b>35,510</b>	<b>36,235</b>	
Impairment Charge	(3,500)	(3,520)	(3,594)	(3,667)	
<b>Pre-tax Profit</b>	<b>27,891</b>	<b>31,265</b>	<b>31,916</b>	<b>32,568</b>	
Tax	(4,817)	(6,253)	(6,383)	(6,514)	
<b>Post-tax Profit</b>	<b>22,750</b>	<b>25,012</b>	<b>25,533</b>	<b>26,054</b>	
<b>Income Statement ('000)</b>	<b>2013A</b>	<b>3Q 2014A</b>	<b>2014E</b>	<b>2015E</b>	<b>2016E</b>
Net interest income	189,263	143,367	195,391	218,689	255,111
Non-interest income	75,091	60,403	77,426	94,388	111,753
<b>Total Revenue</b>	<b>264,354</b>	<b>203,770</b>	<b>272,817</b>	<b>313,077</b>	<b>366,864</b>
Total Operating Costs	(147,196)	(112,394)	(150,049)	(168,138)	(192,385)
<b>Operating Profit</b>	<b>117,158</b>	<b>91,376</b>	<b>122,767</b>	<b>144,939</b>	<b>174,479</b>
Impairment Charge	(11,067)	(4,882)	(8,382)	(14,668)	(19,838)
<b>Pre-tax Profit</b>	<b>106,209</b>	<b>86,818</b>	<b>114,385</b>	<b>130,271</b>	<b>154,641</b>
Tax	(15,279)	(15,772)	(20,589)	(26,054)	(34,021)
<b>Post-tax Profit</b>	<b>90,930</b>	<b>71,046</b>	<b>93,796</b>	<b>104,217</b>	<b>120,620</b>
<b>Balance Sheet ('000)</b>					
<b>Assets</b>	<b>2013A</b>	<b>3Q 2014A</b>	<b>2014E</b>	<b>2015E</b>	<b>2016E</b>
Cash & Short term funds	1,190,292	1,001,815	1,095,003	1,206,554	1,329,168
Due from banks	256,729	426,165	434,950	405,785	526,477
Net Loans	1,251,355	1,526,109	1,427,725	1,689,644	1,953,306
Fixed Assets	69,410	70,951	69,592	99,457	114,452
Other Assets	375,347	383,593	452,348	576,851	654,663
<b>Total Assets</b>	<b>3,143,133</b>	<b>3,408,633</b>	<b>3,479,618</b>	<b>3,978,291</b>	<b>4,578,065</b>
<b>Liabilities</b>					
Deposits	2,276,755	2,309,614	2,549,508	2,913,179	3,367,768
Borrowings	119,678	298,129	114,288	135,497	177,251
Other liabilities	237,449	276,958	266,673	338,742	393,891
<b>Total liabilities</b>	<b>2,633,882</b>	<b>2,884,701</b>	<b>2,930,469</b>	<b>3,387,418</b>	<b>3,938,910</b>
<b>Shareholders' fund</b>	<b>509,251</b>	<b>523,932</b>	<b>549,149</b>	<b>590,873</b>	<b>639,155</b>
<b>Key ratios</b>					
EPS	2.92	2.26	2.97	3.30	3.82
ROE	18%	14%	17%	18%	19%
ROA	2.9%	2.1%	2.7%	2.6%	2.6%
Loan to Asset	40%	45%	41%	42%	43%
Cost to income	56%	55%	55%	54%	52%
Net Profit Margin	29%	27%	26%	25%	25%
Capital adequacy ratio	36%	31%	33%	30%	28%
Liquidity ratio	64%	62%	60%	55%	55%

Source: Company financials, ARM Estimates

## ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6 month period (minimum) to the review date. We adopt a 5 point rating system for this category of stocks and a 3 point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <<1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% — 20 %	NEUTRAL	5% — 20 %
NEUTRAL	0% — 10 %	SELL	<5%
UNDERWEIGHT	-5% — 0%		
SELL	<-5%		

## RECOMMENDATION

### KEY

Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't buy otherwise—subject to reasonable portfolio constraints
UNDERWEIGHT	Minimise exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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