



Equity Research | Zenith Bank Plc

ARM Research

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Full Year Earnings Report

12 months ended 31st December, 2012

Recommendation: NEUTRAL

- Zenith Bank (Zenith) reported 26% YoY growth in gross earnings to N307.1bn for the 12 months ended December 2012. PBT and PAT grew 51% and 107% YoY to N102.1bn and N100.7bn respectively.
- The results embedded further impact of discontinued operations adding N15.2bn to revenue (9M: N12bn), N3.5bn to PBT (9M: N3.2bn) and N2.6bn to PAT (9M: N2.9bn).
- Zenith also announced a N1.60 dividend which translates into a 52% payout ratio exceeding our 45% payout estimate.

Much stronger trading income supports revenues

- On an adjusted basis, Q4 12 revenues were flat QoQ at N74.6bn and 3% ahead of our estimates. Interest income of N53.1 bn in Q4 12 was 7% lower QoQ and 3% below our forecasts as lower asset yields (-80bps QoQ) offset a N170bn rise in total earning assets in Q4 12 to N2.47 trn. We estimated Q4 asset yields at the 9.5% 9M average and factored in more moderate ~ (N50bn) additions to total earning assets.
- The interbank market (Zenith yields ~3%) appeared to be the primary drag on asset yields in line with significant improvement in financial system liquidity in Q4, informing a significant rotation into T-bills (Zenith yields ~11%) which rose 86% to N670bn while interbank assets halved to N182bn.

Income Statement Data

	2012- FY 'm	2011 - FY 'm	%chg
Revenue	307,082	243,948	26%
PBT	102,100	67,440	51%
Tax	(1,419)	(18,736)	-92%
PAT	100,681	48,704	107%

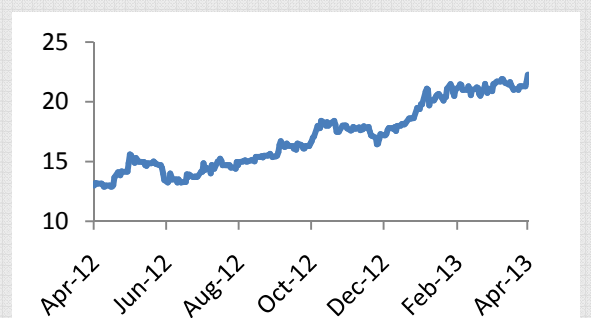
Balance Sheet Data

	2012-Dec 'm	2011 -Dec 'm	%chg
Cash	332,515	223,187	49%
Loans	989,814	893,834	11%
Deposits	1,929,244	1,655,458	17%
Fixed Asset	68,782	68,366	1%
Net Assets	462,956	394,268	17%

Stock Data

Price	N22.28
52 week range	N12.9 - N22.28
Market Cap. (N'm)	699,513.88
1-month Avg. Vol	23,511,388
Curr. PE	6.9x
Bloomberg Ticker	ZENITHBA NL
Reuters Ticker	ZENITHB.LG

Zenith Plc - Share Price Trend



Analyst(s)

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- On the other hand, non-interest revenue (NIR) rose 29% QoQ (22% ahead of our estimates) driven by gains on trading financial instruments (+87% QoQ). This is in line with other Tier 1 banks who have released results so far and probably highlights a renewed industry focus on active trading as Q3 regulatory actions dampened forex gains. Fee income also rose 10% QoQ, as Zenith's intensified efforts to enhance customer service delivery.

Improvements in cost management (and tax credits) underpin margin expansion

- Rapid asset growth was underpinned by 12% QoQ rise in deposits to N1.93 trn which was well ahead of our 2% forecast QoQ growth. Incidentally, breaking a rising trend through 9M 2012, interest expense dipped 7% QoQ to N16.1 bn, driving WACF 40bps lower to 3.2% whereas we anticipated a 10bps increase to 3.7% in view of increased industry competition.
 - Zenith also positively surprised on the opex front with a 13% QoQ contraction in Q4, driving Q4 CIR to 46% (9M avg: 55%). At N26.9bn, Opex was also 10% below our estimates reflecting faster moderation of costs than we envisaged after restructuring earlier in the year. Accordingly, CIR improved a further 130bps to 53% for FY 12, extending the downtrend since Q3 2011.
 - On the flip side, impairment charges increased faster than expected after quadrupling to N2.2bn in Q3. Zenith booked a further N5.1bn in Q4 which still exceeded our N3.1bn estimates, justifying our conservative stance on the issues following significant improvements in view of negative surprises on this front in Q4 2011.
 - With revenues broadly in line, lower opex and interest expense were primarily responsible for Q4 PBT being 25% ahead of our estimates at N26.6bn.
 - Zenith booked a N462mn tax for FY2012 (9M: N10.9bn), implying a tax writeback of N10.4bn in Q4 12. This tax writeback reflects a significant amount of tax exempt income (N37.7bn) and drove Q4 12 PAT of N37bn, 121% greater than our estimates. Applying 9M average tax rate of 15% to Q4 12 PBT would have put Q4 PAT at N22.5bn, 34% ahead of estimates which assumed a 21% tax rate for Q4. Q4 12 PBT and PAT margins of 36% and 50% pushed corresponding FY margins to 34% each, 9pps and 15pps higher than respective
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2011 levels. Adjusted for tax variation, Q4 12 PAT margin would have been 30%.

- FY EPS came in at N3.13 per share for continuing operations while discontinued ops added a further 7k to N3.20 per share.

Improved cost management bolsters forecasts

- Based on weaker interest income QoQ in Q4 being driven by lower asset yields, we expect the rotation into higher yielding securities likely occurred late in the period such that we expect asset yields to recover somewhat in Q1 13. Our forecast for asset yields consequently only incorporates a 50bps decline compared to an 80bps decline in Q4 12. However, this decline is offset by increased earning asset volume estimates--in light of faster than expected deposit growth--which primarily drives our expectation for 12% QoQ growth in interest income for Q1 13. Furthermore, in spite of its surprisingly strong Q4 12, we note that Q1 is traditionally a weak quarter for trading income, underpinning our expectations for a 15% QoQ decline in this metric in Q1 13. Overall, we expect gross earnings to come in 5% higher QoQ at N78.5bn for Q1 2013. A 9% asset yield estimate and unchanged revenue mix from current levels put FY 13E gross revenues at N325bn.
 - We broadly expect cost-management gains to persist but envisage a mild 3% QoQ rise in interest expense on higher volumes whilst keeping WACF flat at current levels. We revise 2013 CIR 100bps lower to 53% en-route our 50% target by 2017, in deference to steady improvement over the past 6 quarters. Nevertheless, this moderation in CIR is largely on account of higher revenue estimates and translates into 20% QoQ forecast opex growth in Q1 2013.
 - We still take a cautious view on provisions though NPL ratio at 3% remains one of the lowest in the industry. We estimate 0.8% cost of risk in line with 2012 levels.
 - Much of the improvements in costs we anticipated for 2013 materialised in 2012 resulting in a more moderate 3% upward revisions to FY 13E PBT and PAT estimates relative to prior, with our adjustments translating to FY 13E EPS of N2.8, which is lower than 2012 figures largely on account of the impact of the exceptional 2012 tax variation where we have applied a 20% FY 13E tax rate. Pro-forma 2013 PAT estimates would be 12% higher YoY otherwise.
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Fair value estimate higher but stock fully valued

- Lower funding costs that apply farther out in our forecasts are the primary driver of enhanced profitability and revisions induced by the base implied by Q4 12 results send our fair value estimates is 26% higher to N24.4 (prev. N19.3). Boosted by the Q4 tax variation, current PE of 6.9x is lower than 10x tier 1 average while our forward PE estimates of 7.9x compare with a 6.5x Tier 1 average and P/Bv of 1.5x with a 1.4x Tier 1 average. Given the 9% upside in our fair value estimate to current market, we maintain our **NEUTRAL** rating on the stock.

Summary of Forecasts

Quarterly					
Income Statement (N'm)	Q1 2013E	Q2 2013E	Q3 2013E	Q4 2013E	
Net interest income	42,869	45,533	44,303	43,099	
Non-interest income	18,702	21,336	20,079	19,560	
Total Revenue	61,571	66,870	64,381	62,659	
Total Operating Costs	(32,448)	(35,871)	(33,929)	(32,390)	
Operating Profit	29,123	30,998	30,452	30,269	
Impairment Charge	(2,645)	(2,842)	(2,765)	(2,721)	
Pre-tax Profit	26,478	28,156	27,687	27,547	
Tax	(5,796)	(5,941)	(5,287)	(4,949)	
Post-tax Profit	20,683	22,215	22,400	22,598	
Annual					
Income Statement (N'm)	2011A	2012A	2013E	2014E	2015E
Net interest income	125,613	156,757	175,804	204,468	231,195
Non-interest income	77,650	70,530	79,677	91,600	105,165
Total Revenue	203,263	227,287	255,481	296,068	336,360
Total Operating Costs	- 118,262	- 119,619	- 134,638	- 153,990	- 172,661
Operating Profit	85,001	107,668	120,842	142,078	163,699
Impairment Charge	- 24,303	- 9,099	- 10,974	- 16,034	- 16,967
Pre-tax Profit	60,698	98,592	109,869	126,044	146,732
Tax	- 16,509	- 462	- 21,974	- 25,209	- 32,281
Post-tax Profit	44,189	98,130	87,895	100,835	114,451
Balance Sheet (N'm)					
Assets					
Cash & Short term funds	739,830	1,001,679	933,227	1,002,666	1,107,541
Due from banks	272,622	182,020	293,533	335,786	427,267
Net Loans	883,147	989,814	1,156,083	1,367,586	1,537,801
Fixed Assets	68,838	68,782	71,944	82,300	92,884
Other Assets	344,182	362,209	423,033	503,679	549,875
Total Asset	2,308,619	2,604,504	2,877,820	3,292,018	3,715,368
Liabilities					
Deposits	1,653,570	1,929,244	2,064,433	2,357,907	2,651,381
Due to banks	-	-	-	-	-
Borrowings	70,136	71,204	71,187	101,445	124,771
Other liabilities	205,386	141,100	237,291	282,400	343,120
Total liabilities	1,929,092	2,141,548	2,372,912	2,741,752	3,119,271
Shareholders' fund	379,527	462,956	504,908	550,265	596,096
Key Data					
EPS Rep GAAP	1.41	3.13	2.79	3.20	3.63
DPS	-	1.60	1.53	1.76	2.18
BVPS	12.09	14.75	16.08	17.53	18.99
ROE	12%	21%	17%	18%	19%
ROA	1.9%	3.8%	3.0%	3.0%	3.1%
Key Ratios					
Loan to Asset	38%	38%	40%	42%	41%
Cost to income	58%	53%	53%	52%	51%
Net Profit Margin	18%	33%	27%	27%	27%
Liquidity ratio	61%	61%	59%	57%	58%
Capital adequacy ratio	29%	31%	30%	32%	33%

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
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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