

Research Update:

Nigeria-Based Zenith Bank PLC Affirmed At 'B-/B' Despite Credit Risk Headwinds From Devaluation; Outlook Stable

September 27, 2023

Overview

- The liberalisation of the foreign exchange regime in June 2023 led to the devaluation of the Nigerian naira and a sharp inflation of Zenith Bank's balance sheet because of its 38% exposure to foreign currency-denominated assets.
- Although Zenith Bank managed to preserve regulatory capital adequacy at 22% thanks to sizable foreign currency revaluation gains, we expect it to operate with lower capital buffers as measured by our risk-adjusted capital model.
- We are affirming our 'B-/B' global scale and 'ngBBB+/ngA-2' national scale ratings on Zenith Bank.
- The stable outlook on Zenith Bank mirrors that on Nigeria.

Rating Action

On Sept. 27, 2023, S&P Global Ratings affirmed its 'B-/B' long and short-term issuer credit ratings on Zenith Bank PLC. The outlook is stable.

At the same time, we affirmed our 'ngBBB+/ngA-2' Nigeria national scale ratings on the bank. Our national scale ratings do not carry an outlook.

Rationale

We expect Zenith Bank to operate with lower capital buffers than before. We believe that Zenith Bank's risk-adjusted capital (RAC) ratio will slide below our 5% threshold and be 4.25%-4.75% over 2024-2025, balancing a sharp increase of risk-weighted assets following the Nigerian naira devaluation, and a strong earnings accretion owing to large currency revaluation gains. That said, Zenith Bank operates with high regulatory capital buffers, above 20% against a

PRIMARY CREDIT ANALYST

Roman Rybalkin, CFA

Dubai

+971 (0) 50 106 1739

roman.rybalkin
@spglobal.com

SECONDARY CONTACTS

Samira Mensah

Johannesburg

+27 11 214 4869

samira.mensah
@spglobal.com

Charlotte Masvongo

Johannesburg

+27 112144816

charlotte.masvongo
@spglobal.com

15% minimum capital adequacy ratio (CAR). The difference between our measure of capitalisation and the bank's CAR stems from comparatively higher capital charges on exposures to Nigerian government securities and our treatment of encumbered assets stemming from the elevated mandatory cash reserves in Nigeria.

We believe Zenith Bank exercised prudence in creating provisions on the back of the currency movement and high inflation. The group utilized a sizable portion of its extraordinary foreign currency revaluation gains in the first half of 2023 to boost provisions for its stage 2 loans as the currency movement inflated the share of stage 2 loans in the total portfolio. The additional 4% provision of its loan book also reflects the higher interest rate environment because of high inflation. We understand that Zenith Bank's provisioning models reflect further weakening of the naira. Despite these provisioning efforts, we expect the cost of risk to stay elevated at 1.5%-2.0%, reflecting challenging operating environment.

At the same time, our view of capital and earnings, combined with our expectations of the bank's portfolio credit sensitivities, is neutral to its 'b+' stand-alone credit profile, which remains two notches higher than its global scale long-term issuer credit rating.

The global scale long-term issuer credit rating on Zenith Bank is constrained by the Nigeria sovereign rating. This reflects the bank's exposure to economic risks of Nigeria, including high direct exposure to sovereign risk through investments in Treasury bills and placements with the central bank, which exceeded 270% of shareholders' equity as of June 30, 2023. We do not rate banks in Nigeria above the 'B-' sovereign long-term foreign and local currency ratings because of the potential direct and indirect implications of sovereign distress on banks' operations and their ability to service foreign currency obligations.

Outlook

The stable outlook on Zenith Bank reflects that on Nigeria.

Downside scenario

If we were to take a negative rating action on Nigeria, we would take a similar negative action on Zenith Bank over the next 12 months.

Upside scenario

A rating action reflecting an improvement of Nigeria's sovereign creditworthiness would result in a similar positive action on Zenith Bank over the next 12 months, all else being equal.

Ratings Score Snapshot

	To	From
Issuer Credit Rating	B-/Stable/B	B-/Stable/B
SACP	b+	b+
Anchor	b	b

	To	From
Issuer Credit Rating	B-/Stable/B	B-/Stable/B
Business position	Strong (+1)	Strong (+1)
Capital and earnings	Constrained (0)	Moderate (0)
Risk position	Adequate (0)	Adequate (0)
Funding and liquidity	Strong and adequate (0)	Strong and adequate (0)
Comparable ratings analysis	0	0
Support	0	0
ALAC support	0	0
GRE support	0	0
Group support	0	0
Sovereign support	0	0
Additional factors	-2	-2

SACP--Stand-alone credit profile.

Related Criteria

- General Criteria: National And Regional Scale Credit Ratings Methodology, June 8, 2023
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Outlooks On 12 Nigerian Banks Revised To Stable After Same Action On Sovereign; Several National Scale Ratings Raised, Aug. 11, 2023
- Nigeria Outlook Revised To Stable From Negative On Reform Initiatives; 'B-/B' Ratings Affirmed, Aug. 4, 2023

Ratings List

Ratings Affirmed

Zenith Bank PLC

Issuer Credit Rating B-/Stable/B

Nigeria National Scale ngBBB+/-/ngA-2

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceld/504352>. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings. Alternatively, call S&P Global Ratings' Global Client Support line (44) 20-7176-7176.

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