

Poised to Deliver Greater Value

Gross Earnings to be Driven by Core Income Lines

For the most part, Zenith Bank Plc (**ZENITHBANK**)'s gross earnings in 2020 were supported by non-core income, particularly FX revaluation gains following the devaluation of the Naira during the period. The bank recorded a 276.44% YoY growth in FX gains which accounted for 65.42% of the growth in gross earnings in 2020FY. Meanwhile, strong growth (+28.57% YtD) in interest earning assets helped keep interest income afloat as the interest rate environment stayed depressed during the period. Trading income was, however, a beneficiary of the relatively low interest rates as the bank was able to book significant capital gains on its investment securities. Expectedly, fee-based income declined significantly by 20.75% YoY owing to the new fee regime on electronic transactions which became effective in January 2020. By and large, the bank's 2020FY gross earnings which grew by 7.53% YoY to NGN696.45bn outperformed our expectations by 4.41%. However, as noted above, growth stemmed mostly from a volatile income line – FX revaluation gains. **Given our outlook for exchange rates this year, we expect gains from FX revaluations to be moderate. On the other hand, we expect an uptick in interest rates, coupled with sustained growth in earning assets to yield a higher growth in interest income. We are also positive about fee-based income growth in view of the bank's retail drive. Our outlook for interest rates implies that we expect trading income to be pressured during the year. Regulatory risk remains the major threat to income growth.**

Risk Asset Repricing to Improve NIM

While the bank's strong assets growth is commendable, it did not translate to a growth in net interest margin (NIM) despite an 18.45% YoY decline in interest expense. This was partly because some of the growth in loan book was due to the translation effect of FCY loans following Naira devaluation. NIM thus fell to 7.90% (vs. 8.20% in 2019FY). After moderating in Q3:2020, impairment charges spiked (+1,117.38% QoQ, +149.89% YoY) in Q4:2020 to provide adequate cover for Stage 3 loans following a significant write-off of NGN53.81bn. **Management has guided that it expects a higher CoR of 2.00% in 2021.** Cost-to-Income ratio inched up to 50.00% (vs. 48.80%) on the back of higher impairment charges, IT spending (to support the business continuity plan triggered by the pandemic), and general inflationary pressure. Although the bottom line grew by 10.40% YoY to NGN230.57bn, supported by lower income tax, both ROAA and ROAE declined marginally to 22.40% and 3.10% respectively. **We expect funding costs to remain within the 3.00% to 3.50% band, while NIM should improve given the current trajectory of interest rates, especially as management has guided that loans will be repriced. Our 2021FY projection for PAT is NGN241.04bn, with an implied growth of 4.54% YoY.**

Solid Prudential Standing to Support Growth

Zenith Bank operates from a solid funding base which continues to support assets growth. While the bank has maintained an excellent prudential standing so far, we are concerned about adverse changes in loan quality due largely to the pandemic. We refer in particular to the reclassification of NGN359.01bn Stage 1 loans to Stage 2 during the period. This could pressure asset quality which currently stands at 4.29% in 2021. Our outlook is consistent with Management guidance of 4.50%.

Recommendation

In view of the above, we have revised our projected **2021FY EPS** to **NGN7.68** from **NGN6.99** while maintaining **Target PE** of **3.85x**. This yields a target price of **NGN29.57**, with an implied upside of **14.38%** based on the closing price on 25th February 2021. Hence, we rate the ticker a **BUY**.

Company	ZENITHBANK
Valuation	
Trailing EPS	NGN7.34
BVPS	NGN35.59
P/E	3.52x
P/BV	0.73x
Target PE	3.85x
Dec-2021 Exp. EPS	7.68
Dec 2021 Target price	NGN29.57
Current Price	NGN25.85
Up/Downside Potential	+14.38%
Ratings	BUY
Key metrics	
ROE	22.40%
ROA	3.10%
Net Margin	33.11%
Asset Turnover	0.08
Leverage	7.59x
Share/Share Price Statistics	
Yr Hi	NGN27.20
Yr Lo	NGN24.10
YTD return	4.23%
Beta	1.39
Adjusted Beta	1.26
52-wk average volume	41,561,991
Shares outstanding	31.40bn
Market cap [NGN]	811.60bn
Financial year end	December
Most Recent Period (MRP)	2020FY



Chart 1: Sensitivity Analysis

Sensitivity Analysis of Dec-2021 Target Price to key model inputs						Min	26.91
						Max	30.73
EPS							
						7.58	7.63
						7.68	7.73
						7.78	
Target PE	3.55x	26.91	27.09	27.26	27.44	27.62	
	3.65x	27.67	27.85	28.03	28.21	28.40	
	3.85x	29.18	29.38	29.57	29.76	29.95	
	3.90x	29.56	29.76	29.95	30.15	30.34	
	3.95x	29.94	30.14	30.34	30.53	30.73	

Financial Highlights (NGN billion) ZENITH BANK PLC 2020FY

<i>Profit & Loss Account</i>	2020FY	2019FY	y/y Growth
Gross Earnings	696.45	647.68	7.53%
Interest Income	420.81	415.56	1.26%
Interest Expense	121.13	148.53	-18.45%
Loan Loss Expense	39.53	24.03	64.51%
Net Interest income after impairment charges	260.15	243.00	7.06%
Non-Interest Income	275.64	232.12	18.75%
Operating Income	535.79	475.12	12.77%
OPEX	256.03	231.83	10.44%
PBT	255.86	243.29	5.17%
PAT	230.57	208.84	10.40%
<i>Balance Sheet</i>	2020FY	2019FY	
Cash and balances with Central Banks	1,591.77	936.28	70.01%
Loans and Advances to customers	2,779.03	2,305.57	20.54%
Investment Securities	2,873.32	2,014.22	42.65%
Property and Equipment	190.17	185.22	2.67%
Other Assets	1,046.99	905.60	15.61%
Total Assets	8,481.27	6,346.88	33.63%
Deposits from customers	5,339.91	4,262.29	25.28%
Financial Liabilities	956.43	754.44	26.77%
Other Liabilities	1,067.45	388.26	174.93%
Total Liabilities	7,363.80	5,404.99	36.24%
Shareholders' fund	1,117.47	941.89	18.64%

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Movements in Price Target

Company Name: Zenith Bank Plc.

Date	Price (N)	Previous Target Price(N)	New Target Price (N)	Previous Recommendation	New Recommendation
26-Feb-2021	25.85	26.91	29.57	HOLD	BUY

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Company	Disclosure
Zenith Bank Plc	

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