

September 29, 2023

ZENITHBANK's Debut into Triple-Digit Earnings Territory

Growth in Funded and Non-Funded Income Support Gross Earnings

Riding on the positive wave in the Nigerian banking industry, Zenith Bank Plc. (ZENITHBANK) reported an impressive 138.97% YoY growth in its gross earnings to NGN967.26bn in H1:2023. This growth was driven by the funded and non-funded income stream improvement. The interest income stream benefitted from the impact of loan volume growth, the repricing of loan terms leading to higher lending rates and improved interest from investment securities. Consequently, asset yield rose by 180bps to 5.38% (vs 3.58% in H1:2022), pushing interest income up by 71.86% YoY to NGN415.43bn. Meanwhile, non-interest income grew significantly by 246.15% YoY to NGN515.69bn, owing to higher recovery of impaired and written-off loans (+240.58% YoY) as well as net FX revaluation gain (c.69% of non-interest income). Additionally, higher trading activities supported trading income (+20.93% YoY), while net fees and commission income declined by 31.85% YoY. **We anticipate that growth in the bank's loan portfolio and better yields on investment securities will prompt an uptick in interest income. Moreover, the expected rise in transaction volumes across the bank's digital platforms, higher trading income, and FX revaluation gains will push non-funded income upward. As a result, we forecast a 58.30% YoY growth in gross earnings to NGN1.50trn in 2023FY.**

Macro Shocks and Bottomline Growth

Although the higher CASA mix (36.62% vs 32.76% in H1:2022) reported in H1:2023, the combined effect of the prevailing high-interest rate environment and 29.37% YtD increase in interest-bearing liabilities pushed ZENITHBANK's cost of funds up by 70bps to 2.60%. Thus, interest expense jumped by 169.49% YoY to NGN153.56bn. Consequently, the net interest margin narrowed by 123bps to 5.89%. Owing to the current inflationary pressures and annual salary review, higher regulatory cost (+30.39% YoY), personnel expenses (+44.58% YoY), advertisement & promotions (+30.90% YoY), and outsourcing services (+54.68% YoY) drove operating expenses up by 22.77% YoY to NGN219.27bn. Additionally, the bank recognized a significant impairment charge of NGN207.93bn (vs NGN25.12bn in H1:2022) on its loans in response to the deteriorating macroeconomic conditions. Thus, the cost of risk ballooned to 8.78% (vs 1.42% in H1:2022). Notwithstanding, the improvement in operating income was enough to suppress the cost-to-income ratio by 1946bps to its lowest level (38.47%) in over a decade. Consequently, Profit After Tax (PAT) grew by 161.85% YoY to NGN291.73bn. **Considering our expectation that inflationary pressures will linger in the operating environment, we anticipate a further uptick in operating expenses. Nevertheless, we expect a boost in operating income to mute higher personnel expenses, impairment charges, and operational costs. Consequently, we project a 74.25% YoY growth in PAT to NGN390.16bn in 2023FY.**

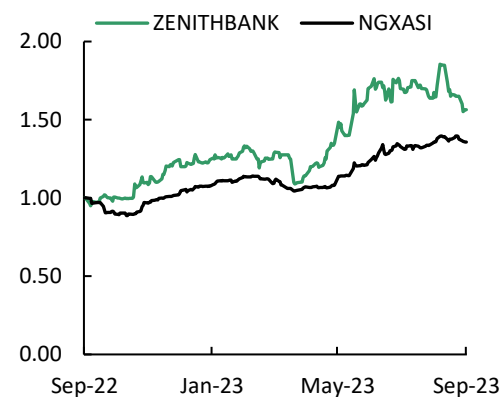
Robust Prudential Ratios

The bank's gross loan stock grew by 30.48% YtD to NGN5.38trn, driven mainly by the upward revaluation of foreign currency (FCY) loans. Amidst the challenging macroeconomic landscape, ZENITHBANK's strategic currency composition of its loan book minimized its exposure to credit impairment. Thus, non-performing loan (NPL) and NPL coverage ratios improved by 40bps and 85bps to 3.92% and 201.10%, respectively. Furthermore, the capital adequacy ratio rose by 320bps to 22.00%, while the liquidity ratio declined to 61.00% from 75.00% in H1:2022. **Overall, the bank's key prudential metrics remain adequate and comfortably above the regulatory limits.**

Recommendation

Following our PAT forecast, we revised our expected 2023FY EPS upward to NGN12.43. Combining this with a Target PE of 3.06x, we arrive at a target price of NGN38.03. Compared to the closing price on 29th September 2023, this translates to an upside potential of **+21.05%**. Thus, we rate the ticker a **BUY**.

Company	ZENITHBANK
Valuation	
Trailing EPS	12.88
BVPS	56.76
P/E	2.56
P/BV	0.58
Target PE	3.06x
Dec-2023 Exp. EPS	NGN12.43
Dec 2023 Target price	NGN38.03
Current Price	NGN31.45
Up/Downside Potential	+20.91%
Ratings	BUY
Key metrics	
ROE	22.68%
ROA	2.52%
Net margin	26.81%
Asset Turnover	0.09x
Leverage	9.00x
Yr Hi	NGN37.10
Yr Lo	NGN21.80
YTD return	+30.42%
Beta	0.88
Adjusted Beta	0.90
Proposed DPS	NGN0.50
Shares outstanding	31.40bn
Market cap [NGN]	982.71bn
Free Float	87.98%
Financial year end	December
Most Recent Period	H1:2023



Analyst:

Matilda Adefalajo

matildaadefalajo@meristemng.com

+234 (903) 038 4160

Chart 1: Sensitivity Analysis

Sensitivity Analysis of Dec-2023 Target Price to Key Model Inputs						Min	30.53
						Max	46.02
						EPS	
						11.93	12.18
						12.43	12.68
						12.93	
Target PE	2.56x	30.53	31.17	31.81	32.45	33.09	
	2.81x	33.51	34.22	34.92	35.62	36.32	
	3.06x	36.50	37.26	38.03	38.79	39.56	
	3.31x	39.48	40.31	41.13	41.96	42.79	
	3.56x	42.46	43.35	44.24	45.13	46.02	

Financial Highlights and Forecasts (NGN billion)

<i>Profit & Loss Account</i>	H1:2022	H1:2023	2023F	2024F	2025F	2026F	2027F
Gross Earnings	404.76	887.20	1,496.79	1,621.75	1,746.94	1,859.48	1,973.42
Interest Income	241.73	415.43	718.50	863.49	945.76	1,021.24	1,095.67
Interest Expense	56.98	173.54	266.44	335.35	363.79	391.95	421.34
Net Impairment Charges	59.93	153.56	210.90	250.76	208.57	204.04	191.04
Net Interest income after impairment charges	159.62	53.94	241.16	277.37	373.40	425.26	483.30
Non-Interest Income	163.04	471.77	778.29	758.26	801.19	838.23	877.75
Operating Income	287.85	560.09	1,019.45	1,035.64	1,174.59	1,263.49	1,361.05
OPEX	178.60	219.27	457.58	517.36	524.67	556.64	589.49
PBT	280.37	284.65	499.88	453.19	581.58	635.10	696.22
PAT	111.41	291.73	390.16	353.72	453.92	508.08	556.97

<i>Balance Sheet</i>	2022FY	H1:2023	2023F	2024F	2025F	2026F	2027F
Cash and Balances with Central Banks	1,630.36	2,730.35	3,027.50	3,840.04	4,956.53	5,541.74	6,932.74
Loans and Advances to Banks and customers	3,499.02	5,051.67	5,663.63	5,963.92	6,339.08	6,728.44	7,242.67
Investment Securities	1,482.93	2,023.18	2,078.71	2,138.82	2,200.71	2,285.81	2,374.30
Property and Equipment	202.28	230.84	255.81	293.14	329.96	356.41	379.92
Other Assets	205.17	522.41	613.42	700.83	607.31	693.56	842.04
Total Assets	10,115.36	16,031.91	17,407.34	18,907.32	20,388.85	21,908.84	23,547.64
Deposits from Banks and Customers	7,152.96	11,626.11	12,772.33	13,902.76	14,903.36	16,124.49	17,337.79
Financial Liabilities	553.37	787.85	754.19	769.27	784.66	800.35	816.36
Other Liabilities	8,843.09	14,249.93	15,471.92	16,790.78	18,092.00	19,397.46	20,798.12
Total Liabilities	1,272.28	1,781.98	1,935.42	2,116.54	2,296.85	2,511.38	2,749.53
Shareholders' fund	1,630.36	2,730.35	3,027.50	3,840.04	4,956.53	5,541.74	6,932.74

<i>Financial Ratios</i>	2021FY	2022FY	2023F	2024F	2025F	2026F	2027F
Asset Yield	3.58%	5.38%	8.52%	7.92%	8.27%	8.34%	8.37%
Cost of Funds	1.50%	1.42%	2.30%	2.20%	2.20%	2.20%	2.20%
Net Interest Margin	3.21%	3.39%	4.35%	4.15%	4.62%	4.75%	4.81%
Cost to Income Ratio	62.05%	39.15%	44.89%	49.96%	44.67%	44.06%	43.31%
Net Margin	27.53%	32.88%	26.07%	21.81%	25.98%	27.32%	28.22%
Return on Asset	1.14%	2.06%	2.63%	1.95%	2.31%	2.40%	2.45%
Return on Equity	8.73%	18.46%	23.54%	17.46%	20.57%	21.13%	21.17%
Earnings Per Share	3.55	9.29	12.43	11.27	14.46	16.18	17.74
Asset Turnover	0.04x	0.06x	0.10x	0.09x	0.09x	0.09x	0.09x
Financial Leverage	7.95x	9.00x	8.99x	8.93x	8.88x	8.72x	8.56x

Contact Information

Brokerage and Retail Services

topeoludimu@meristemng.com
 adaezeonyemachi@meristemng.com
 contact@meristemng.com

(+234 905 569 0627)
 (+234 808 369 0213)

Investment Banking/Corporate Finance

rasakisalawu@meristemng.com
 davidadu@meristemng.com

(+234 806 022 9889)
 (+234 810 940 4836)

Wealth Management

funmilolaadekola-daramola@meristemng.com
 crmwealth@meristemng.com
 Tel: +234 01 738 9948

(+234 805 498 4522)

Registrars

oluseyiowoturo@meristemregistrars.com
 www.meristemregistrars.com
 Tel: +23401-280 9250

(+234 802 321 0561)

Trust Services

damilolahassan@meristemng.com
 trustees@meristemng.com

(+234 803 613 9123)

Finance

olasokomubo@meristemfinance.com
matthewawotundun@meristemfinance.com

(+234 803 324 7996)
 (+234 802 390 6249)

Group Business Development

sulaimanadedokun@mersitemng.com
 ifeomaanyanwu@meristemng.com
 info@meristemng.com

(+234 803 301 3331)
 (+234 802 394 2967)

Client Services

adefemitaiwo@meristemng.com
 car@meristemng.com

(+234 803 694 3034)

Investment Research

damilarejo@meristemng.com
 praiseihansekhien@meristemng.com
 research@meristemng.com

(+234 816 890 2771)
 (+234 817 007 1512)

Corporate websites: www.meristemng.com www.meristemwealth.com www.meristemregistrars.com

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Asset allocation: The recommended weighting for equities, cash and fixed income instrument is based on a number of metrics and does not relate to a particular size change in one variable.

Movements in Price Target

Company Name: Zenith Bank Plc.

Date	Price (N)	Previous Target Price(N)	New Target Price (N)	Previous Recommendation	New Recommendation
07-July-2023	34.80	26.69	31.49	BUY	HOLD
29-Sep-2023	31.30	31.49	38.03	HOLD	BUY

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