Nigeria | Equity Research | Banks | Company Update

June 14, 2022

ZENITH BANK PLC

Leveraging retail to boost margin

BLOOMBERG: ZENITHBANK NL

BUY

Target Price: N30.23

Ref Price: N22.70

Our 12-month target price (TP) for ZENITHBANK is mostly unchanged at N30.23 (vs N29.86 in our previous publication). Our TP is likely to be supported by the bank's strategy of accelerated retail penetration, which could combine with the passthrough from robust growth in interest-earning assets to amplify the impact of higher yields on earnings. We see scope for a capital appreciation of 32.3% and a dividend yield of 15.2% over the next 12 -months. We retain a BUY recommendation on the ticker on the back of this projected upside and an implicit undervaluation by the market.

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Net interest income is likely to be the fulcrum for earnings.

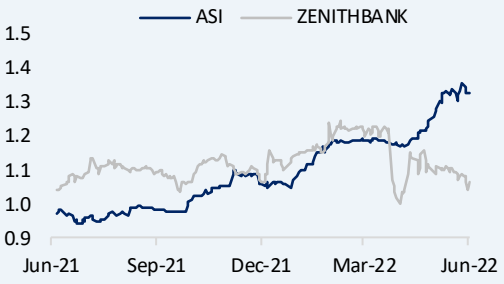
In our view, ZENITHBANK could grow earnings by 8.0% YoY to N264.2 billion in FY'22, aided by a projected improvement in net interest income (NII). The support from NII is likely to be inspired by:

1. the effect of robust growth in interest-earning assets (Q1'22: 21.3% YoY vs 5-year CAGR: 14.8%)
2. the potential impact of higher yield on fixed-income investments
3. a largely contained increase in the cost of funds (CoF) due to the passthrough from its aggressive retail drive.

In line with our position, ZENITHBANK reported an over 20.0% growth in Q1'22 NII that fed off the surge in interest-earning assets and a 90 bps improvement in asset yields. Given that the Q1'22 performance preceded the May 2022 MPC rate action, our expectation for NII now appears mostly conservative. To shed some light on point 3, we note that the bank boasts the highest low-cost deposit ratio (92.6%) across our coverage with a better propensity to withstand the negative impact of interest-rate changes on the cost of funds. We have an FY'22 CoF forecast of 1.7% vs 1.6% in FY'21, with NIMs likely to come in 10 bps higher YoY at 5.3%.

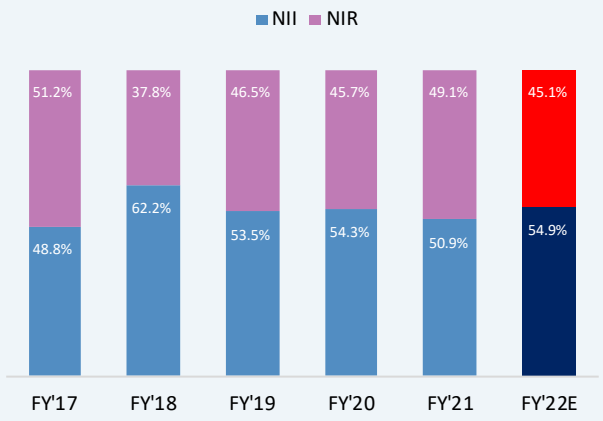
Market Data	ZENITHBANK
Market Cap (N'bn)	712.7
Last close price (N)	22.70
52-week high-low price (N)	27.40/22.00
Avg 3M daily volume (mn)	15.7

1-year price performance (rebased)



Source: NSE; CardinalStone Research

Figure 1: NII to remain the dominant income support in FY'22



Source: Company Financials; CardinalStone Research

However, we have a cautious stance on NIR due to the potential impact of a contraction in foreign exchange gain, a likely pass-through from naira appreciation relative to the 31st December 2021 close for the USD/NGN. That said, we note that expectations for improved volatility in the fixed income space are likely to support trading gains and provide a consequent offsetting effect.

Retail momentum to continue in FY'22

In line with management's guidance, we see scope for improved contribution from the higher-margin retail segment. To this point, we note that retail PBT margin approximated 55.1% in FY'21 (vs 36.0% for the next best margin segment).

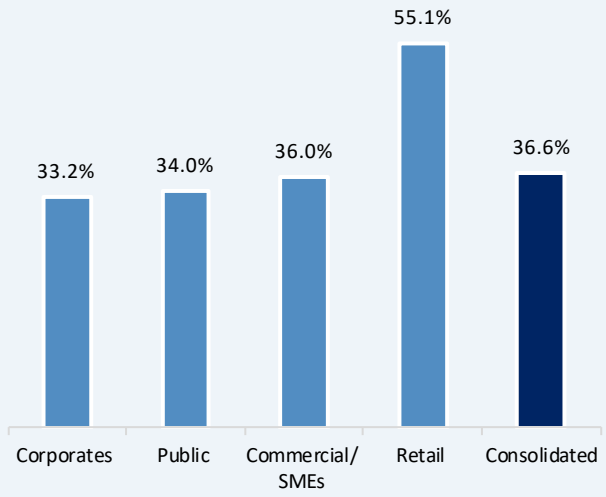
Management has highlighted its willingness to continue chasing this low-cost retail strategy through the continuous expansion of retail-focused loans (+1.5ppts YoY to 5.7% in FY'21). For FY'22, management intends to build momentum on this front through the following initiatives:

1. The continued leveraging of the Zenith Bank Intelligent Virtual Assistant (ZIVA)
2. The deepening of retail market penetration using its digital platforms
3. The increasing volume of processed transactions on its digital platforms

While we commend management's stance on retail penetration, we are wary of its significant geographical concentration risk relative to tier 1 peers (Nigerian business accounts c.88.0% and 98.0% of the bank's total revenue and PAT, respectively).

Our model adjustments translate to an average ROE of 19.5% across our forecast horizon (vs prior 5-year mean of 22.0%). PAT is also likely to print at N264.2 billion in FY'22 and reach N378.2 billion in FY'26E. Elsewhere, the bank remains adequately capitalized with CAR at 21.0% and liquidity ratio at 71.6%. We believe these ratios bode well for improved risk asset creation (FY'22 loan guidance: 10.0%).

Figure 2: Retail PBT margin exceeds other segments'



Source: Company Financials; CardinalStone Research

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Valuation summary

ZENITHBANK is trading at a forward PB of 0.5x, compared to its 4-year mean of 0.8x. Our 12-month TP of N30.23 implies an exit PB of 0.7x and a potential 32.2% upside compared to our reference price of N22.70.

Figure 3: ZENITHBANK is trading at 1 S.D over its 5-year mean P/B



Source: Capital IQ; CardinalStone Research

Income Statement	2020A	2021A	2022F	2023F	2020A	2021A	2022F	2023F
		(N'Mn)				($'Mn)		
Gross Earnings	672,558	736,632	811,216	901,963	1,621	1,775	1,955	2,173
Interest Income	420,813	427,597	500,751	563,727	1,014	1,030	1,207	1,358
Interest expense	(121,131)	(106,793)	(126,207)	(141,250)	(292)	(257)	(304)	(340)
Net interest income	299,682	320,804	374,544	422,477	722	773	903	1,018
Non-interest income	251,745	309,035	310,465	338,236	607	745	748	815
Loan loss provisions	(39,534)	(59,932)	(45,384)	(53,591)	(95)	(144)	(109)	(129)
Operating expenses	(256,032)	(289,533)	(328,805)	(365,142)	(617)	(698)	(792)	(880)
Pre-tax earnings	255,861	280,374	310,821	341,979	617	676	749	824
Taxation	(25,296)	(35,816)	(46,623)	(51,297)	(61)	(86)	(112)	(124)
Profit after tax	230,565	244,558	264,197	290,682	556	589	637	700
Statement of Financial Position	**2020A**	**2021A**	**2022F**	**2023F**	**2020A**	**2021A**	**2022F**	**2023F**
Assets								
Cash and cash equivalents	1,591,768	1,488,363	1,810,983	2,026,154	3,836	3,586	4,364	4,882
Investments Securities	3,728,311	4,208,696	4,602,649	4,845,371	8,984	10,141	11,091	11,676
Loans and Advances	2,779,027	3,355,728	3,633,000	3,982,315	6,696	8,086	8,754	9,596
Other Assets	191,996	195,048	236,897	241,497	463	470	571	582
Property and Equipment	190,170	200,008	217,980	238,132	458	482	525	574
Total Assets	8,481,272	9,447,843	10,501,510	11,333,469	20,437	22,766	25,305	27,310
Liabilities								
Customer deposits	5,339,911	6,472,054	7,266,001	7,819,998	12,867	15,595	17,508	18,843
Trading Liabilities & Due from	11,076	14,674	41,911	84,971	27	35	101	205
Other Liabilities	1,131,042	902,472	961,264	1,011,987	2,725	2,175	2,316	2,439
Current income tax payable	11,690	28,512	28,512	28,512	28	69	69	69
Borrowings	870,080	750,469	768,128	779,321	2,097	1,808	1,851	1,878
Total Liabilities	7,363,799	8,168,181	9,065,816	9,724,789	17,744	19,682	21,845	23,433
Capital and Reserves								
Common equity	1,116,499	1,278,518	1,434,719	1,607,706	2,690	3,081	3,457	3,874
Minority interest	974	1,144	974	974	2	3	2	2
Shareholders' funds	1,117,473	1,279,662	1,435,693	1,608,680	2,693	3,084	3,460	3,876
Total liabilities and equity	8,481,272	9,447,843	10,501,510	11,333,469	20,437	22,766	25,305	27,310
Key Ratios	**2020A**	**2021A**	**2022F**	**2023F**	**2020A**	**2021A**	**2022F**	**2023F**
Profitability								
Cost of Funds	2.2%	1.6%	1.7%	1.7%	2.2%	1.6%	1.7%	1.7%
Cost of Risk	1.4%	1.7%	1.2%	1.3%	1.4%	1.7%	1.2%	1.3%
Non-Performing Loan ratio	6.4%	3.9%	5.3%	4.5%	6.4%	3.9%	5.3%	4.5%
Return on Average Equity	22.4%	20.4%	19.5%	19.1%	22.4%	20.4%	19.5%	19.1%
Return on Average Assets	3.1%	2.7%	2.6%	2.7%	3.1%	2.7%	2.6%	2.7%
Valuation Multiples								
P/E (x)	3.1	2.9	2.7	2.5	3.1	2.9	2.7	2.5
P/B (x)	0.6	0.6	0.5	0.4	0.6	0.6	0.5	0.4

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