

Impressive Performance as Zenith Bank Records Double-Digit Growth in the Topline

INVESTMENT SUMMARY

Zenith Bank maintained outstanding performance in nine-month to September 2022 as gross earnings grew significantly by 16.95% to ₦620.57 billion (vs. ₦518.67 billion in nine-month to September 2021), driven by the solid growth in the two major income lines (interest income and non-interest income). The total interest income grew by 26.52% to ₦390.76 billion in 9M'22 (vs. ₦308.84 billion in 9M'21), driven mainly by the growth bank's risk assets and improvement in pricing. In addition, the non-interest income of the bank improved by 9.96% to ₦211.97 billion in 9M'22 (vs. ₦192.77 billion in 9M'21), driven by deposit growth and improvement in electronic banking income. Meanwhile, the high yield environment and growth in funding base resulted in interest and similar expenses of ₦107.85 billion in 9M'22, which is 45.55% higher than ₦74.10 billion recorded in 9M'21. The operating expenses also grew by 16.95% to ₦255.23 billion in 9M'22 (vs. ₦218.91 billion in 9M'21) due to the inflationary pressure and rising cost of doing business in the country.

The strong growth in the loan book of the bank resulted in higher impairment charge as it increased by 28.81% to ₦37.10 billion in 9M'22 (vs. ₦28.80 billion in 9M'21). The growth in the two major income lines of the bank aided the bottom line as profit before tax grew by 12.65% to ₦202.55 billion in 9M'22 (vs. ₦197.81 billion in 9M'21). However, the bank made higher provision of ₦28.22 billion for tax in 9M'22 (9M'21: ₦19.22 billion). Notwithstanding the higher tax provision during the period, the profit after tax grew 8.55% to ₦174.33 billion in 9M'22 (vs. ₦160.59 billion in 9M'21), which resulted in a 12-month trailing earnings per share of ₦8.23. Based on the recent figures released by the bank and positive outlook in the coming quarters, we maintain a **STRONG BUY** rating on the stock at the current price of ₦21.80 as present forward estimate places the company share price at ₦30.38 (Previous Target Price: ₦31.14).

Table 1: Quarterly results highlights

	3Q2022	2Q2022	3Q2021	Q/q Δ	Y/y Δ
Gross Earnings (₦mn)	215,811	213,240	173,114	+1.21%	+24.66%
Net Int. Income (₦mn)	98,164	84,204	74,806	+16.58%	+31.22%
Net profit (₦mn)	62,918	53,215	54,475	+18.23%	+15.50%

Source: NGX, Bloomberg, PAC Research

November 17, 2022

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Price:

- Current	₦21.80
- Target	₦30.38
Recommendation:	STRONG BUY

* As at Wednesday November 16, 2022

Table 2: Stock data

	December
FYE	December
Price Mov't: YtD / 52wk	-20.48%/-16.67%
52-week range	₦27.50 - ₦18.90
30-day Average vol.	9,212,084
Shares Outstanding (mn)	31,396.49
Market Cap. (₦bn)	626.36
12-Month Trailing EPS (₦)	8.23
DPS (₦) - FY2021	3.10

Source: NGX, Bloomberg, PAC Research

Table 3: Key ratios

	9M'22	9M'21
Net Interest Margin	6.20%	6.80%
Net Profit Margin	28.09%	30.96%
Equity Multiplier	8.67	7.37
Cash/ Total Assets	16.50%	18.07%

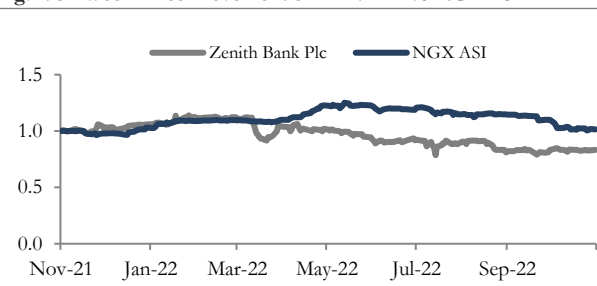
Source: NGX, PAC Research

Tab 4: Valuations

	FY2020	FY2021	FY2022E	FY2023F
P/E (x)	2.97	2.80	2.67	2.51
P/B (x)	0.61	0.53	0.56	0.50
Div Yield	13.76%	14.22%	14.68%	15.14%
Payout Ratio	40.85%	39.80%	39.26%	37.94%
EV/Revenue	1.57	1.11	1.08	1.18
Rev per share	22.18	24.38	26.94	28.83
ROE	20.63%	19.11%	21.05%	20.05%
ROA	2.72%	2.59%	2.26%	2.15%

Source: NGX, PAC Research

Fig. 1: 52-Week Price Movement of ZENITH vs NGX ASI



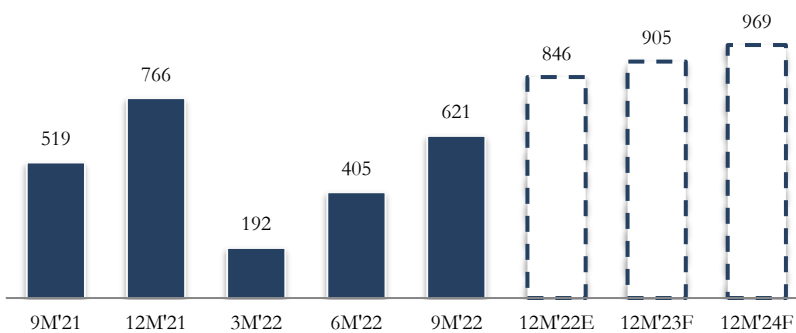
Source: Bloomberg, PAC Research

Gross earnings grow by 20% year-on-year, driven by double-digit growth in interest income and non-interest income: In line with our expectations, the two major income lines of Zenith Bank continued with impressive performance in the third quarter of 2022. The strong growth in the interest income and non-interest income of the bank raised the gross earnings by 19.65% to ₦620.57 billion in nine-month to September 2022 (vs. ₦518.57 billion recorded in nine-month to September 2021). Due to the growth in risk assets and an improvement in pricing, the interest income of the bank increased by 26.52% to ₦390.76 billion in 9M'22 (vs. ₦308.84 billion in 9M'21). In addition, the non-interest income of the bank improved by 9.96% to ₦211.97 billion in 9M'22 (vs. ₦192.77 billion in 9M'21), driven by deposit growth and improvement in electronic banking income.

We maintain that the gross earnings of Zenith bank will continue to improve in the remaining quarter of the years due to the expectation of continuous growth in risk assets and recent rise in policy rate in the country. In addition, we maintain that increased patronisation and improved transaction in electronic banking, such as POS, agency banking, mobile banking, internet banking and ATM transactions, will continue to raise non-interest income of the bank in the remaining quarter of the year. Meanwhile, the recent move to redesign selected local bank notes, which led to the suspension of bank charges on cash deposits (for the purpose of transition from existing to new notes) is expected to have impact on the non-interest income of the bank.

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Fig. 2: Gross Earnings – 9M'21 – 12M'24F (Billion NGN)



Source: NGX, PAC Research

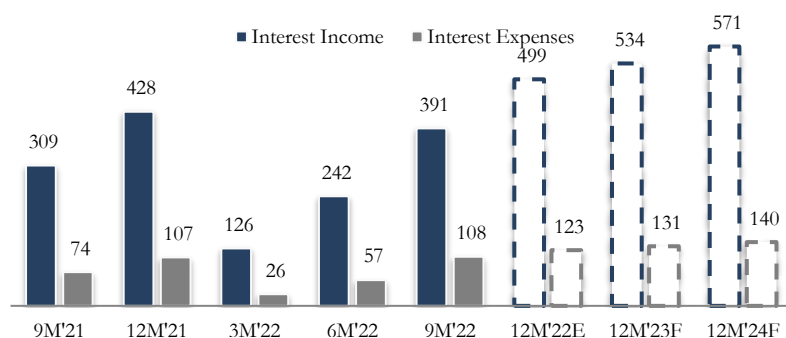
Interest income rises by 27% year-on-year, driven by growth in risk assets and an improvement in pricing: Zenith bank continued to benefit from the decision of the Central Bank of Nigeria (CBN) to raise Monetary Policy Rate to 15.50% in the second half of 2022. The higher policy rate had positive impact on yields on risk assets of the bank during the period. In addition, the bank recorded impressive growth in the risk asset in nine-month to September 2022.

The strong growth in risk assets and improvement in pricing resulted in higher interest income from loans and advances, treasury bills, commercial papers and bonds. Interest income from loans and advances increased by 26.29% to ₦261.25 billion in 9M'22 (vs. ₦206.86 billion in 9M'21). In addition, interest income from treasury bills and bonds increased by 6.63% and 39.72% to ₦33.68 billion in (9M'21: ₦31.58 billion) and ₦86.43 billion (9M'21: ₦61.86 billion) in 9M'22 respectively. Consequently, the total interest income of the bank increased significantly by 26.52% to ₦390.76 billion in 9M'22 (vs. ₦308.84 billion in 9M'21).

Meanwhile, the high yield environment raised the cost of funds by 30 basis point to 1.7% in 9M'22 (9M'21: 1.4%). This affected the net interest margin (NIM) which dropped to 6.2% in 9M'22 (9M'21: 6.8%) due to the implementation of higher yields on interest-bearing liabilities. The high cost of funds, in addition to the growth in funding base, raised the interest and similar expenses significantly by 45.55% to ₦107.85 billion in 9M'22 (vs. ₦74.10 billion in 9M'21). Specifically, the total interest and similar expenses on current account, savings accounts and time deposits increased by 71.93%, 52.41% and 28.94% to ₦11.60 billion (9M'21: ₦6.74 billion), ₦18.11 billion (9M'21: ₦11.88 billion), and ₦31.28 billion (9M'21: ₦24.26 billion) in 9M'22 respectively. In addition, the interest expenses on borrowed funds increased by 42.93% to ₦44.61 billion in 9M'22 (vs. ₦31.21 billion in 9M'21).

With the hike in the country's policy rate and expectation of improved interest-earning assets, we may continue to see improvement in the interest income of the bank in the fourth quarter of 2022. However, the elevated yield environment and expectation of growth in funding base are expected to raise the interest expenses in the fourth quarter of 2022.

Fig. 3: Interest Income and Interest Expenses: 9M'21 – 12M'24F (Billion NGN)



Source: NGX, PAC Research,

The strong growth in risk assets and improvement in pricing resulted in higher interest income from loans and advances, treasury bills, commercial papers and bonds

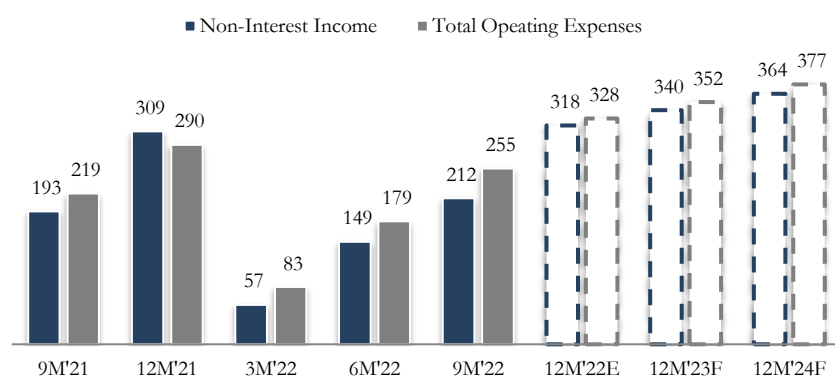
Non-interest income grows by 10% (year-on-year), driven mainly by strong growth in electronic products and account maintenance fees: In nine-month to September 2022, the non-interest income of Zenith Bank increased significantly by 9.96% to ₦211.97 (vs. ₦192.77 billion recorded in nine-month to September 2021). According to the bank, the growth in non-interest income was enabled by the group's retail strategy, with continued strong customer acquisition driving transactions, deposit growth and growth in electronic banking income. Specifically, income from fee on electronic products increased significantly by 50.33% to ₦36.07 billion in 9M'22 (vs. ₦23.99 billion in 9M'21) due to improved transaction in internet banking, mobile banking, POS and USSD. In addition, the strong customer acquisition resulted in higher income from account maintenance fee which increased by 16.36% to ₦28.15 billion in 9M'22 (vs. ₦24.19 billion in 9M'21).

However, the total operating expenses of the bank grew by 16.59% to ₦255.23 billion in 9M'22 (vs. ₦218.91 billion in 9M'21), mainly driven by inflationary pressure and the rising cost of doing business in the country. This resulted in higher cost to income ratio of 55.8% in 9M'22 (9M'21: 54.9%). Although, the operating expenses increased by 16.59%, this is lower than the inflation rate of 20.77% for the month September 2022. This showed the effort of the management in upholding its cost minimisation strategy.

With the increased awareness in electronic banking and expectation of strong customer acquisition, the non-interest income of the bank is expected to maintain upward trend. Due to the assumption of rising inflation and rising cost of doing business within the country, we maintain that the bank will continue to witness increase in the operating expenses.

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Fig. 4: Non-Int. Income & Total Op. Expense: 9M'21 – 12M'24F (Billion NGN)

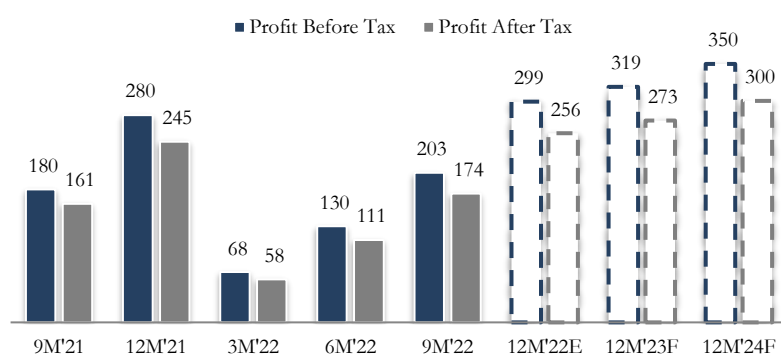


Source: NGX, PAC Research

Despite the significant increase in impairment charge and tax provision, net profit grows by 9% (year-on-year): The strong growth in the loan book of the bank during the period under review resulted in higher impairment charge as it increased by 28.81% to ₦37.10 billion in 9M'22 (vs. ₦28.80 billion in 9M'21).

Meanwhile, the growth recorded in the major income lines of the bank outweighed the increase in operating expenses, interest expenses and impairment charge during the period. Subsequently, profit before tax increased by 12.65% to ₦202.55 billion in 9M'22 (vs. ₦179.81 billion 9M'21). Meanwhile, the resumption of tax collection on income tax on bonds, and short-term securities continued to raise the tax provision of the bank, which increased by 46.85% to ₦28.22 billion in 9M'22 (9M'21: ₦19.22 billion). Despite the higher tax provision, net profit grew by 8.55% to ₦174.33 billion in 9M'22 (vs. ₦160.59 billion in 9M'21), translated to a 12-month trailing earnings per share (EPS) of ₦8.23.

Fig. 5: PBT, Taxation and PAT – 9M'21 – 12M'24F (Billion NGN)



Source: NGX, PAC Research

Zenith Bank maintains a strong balance sheet in Q3'21: expectation of impressive dividend payment in FY'22:

In the third quarter of 2022, Zenith Bank maintained solid and strong balance sheet as the liquidity ratio and capital adequacy ratio of the bank in the third quarter of 2022 are well above the regulatory requirement of 30% and 16% respectively. In the third quarter of 2022, the liquidity ratio of the bank increased to 66.2% (Q3'21: 50.9%), while the capital adequacy ratio remained at 19.1% (Q3'21: 20.1%). However, the bank recorded a loan-to-deposit ratio of 56.5% in Q3'22 (Q3'21: 62.6%), which is below the regulatory minimum requirement of 65.0%, as the bank continued to monitor its loans and advances.

The total assets grew by 29.60% to ₦11.34 trillion in third quarter of 2022 (vs. ₦8.75 trillion in the third quarter of 2021), mainly driven by higher cash and cash balances with Central Bank, improved loans and advances to customers, higher treasury bills, strong growth in investment securities, among others. Mainly because of significant increase in the mandatory reserve deposits with central bank, the cash and cash balances increased by 18.33% to ₦1.87 trillion in Q3'22 (vs. ₦1.58 trillion in Q3'21). In addition, the loans and advances increased significantly by 28.46% to ₦3.88 trillion in Q3'22 (vs. ₦3.02 trillion in Q3'21) as the bank continued to pursue the regulatory minimum loan-to-deposit ratio of 65%.

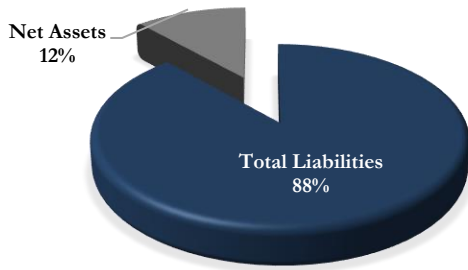
...liquidity ratio and capital adequacy ratio of the bank in the third quarter of 2022 are well above the regulatory requirement of 30% and 16% respectively

However, the total liabilities of the bank rose by 32.64% to ₦10.03 trillion in Q3'22 (vs. ₦7.56 trillion in Q3'21), mainly boosted by improved deposits from customers and higher borrowings. The deposits from customers increased significantly by 33.13% to ₦8.04 trillion in Q3'22 (vs. ₦6.04 trillion in Q3'21) due to the confidence the market has in the brand. In addition, the borrowings increased by 85.59% to ₦1.05 trillion in Q3'22 (vs. ₦0.57 trillion in Q3'21) The increase in borrowings is attributed mainly to increase in Due to Banks for Clean Letters of Credit and new Due to Standard Chartered Bank.

Consequently, the net asset of the bank increased by 10.24% to ₦1.31 trillion in Q3'22 (vs. ₦1.19 trillion in Q3'21), which translated to a higher net asset per share of ₦41.68 (Q3'21: ₦37.81). With the impressive financial position and progressive operating performance, we expect the bank to reward the shareholders with impressive dividend payment in the full year of 2022. (fig. 7)

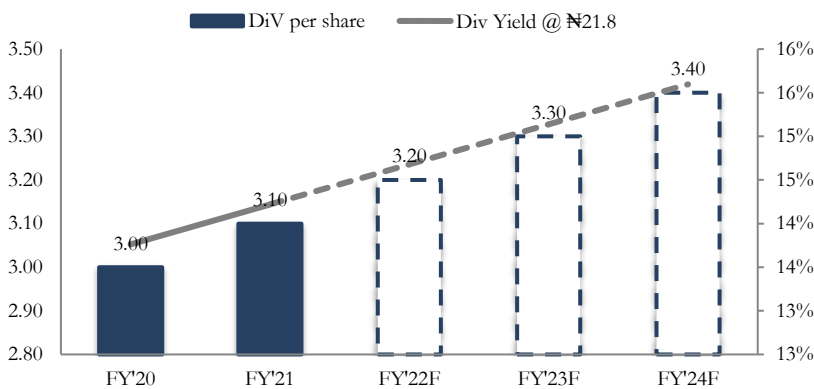
With the impressive financial position and progressive operating performance, we expect the bank to reward the shareholders with impressive dividend payment...

Fig. 6: Total Liabilities Vs Net Asset in Q3'22



Source: NGX, PAC Research

Fig. 7: Dividend Per Share and Dividend Yield (FY'20-FY'24F)



Source: NGX, PAC Research

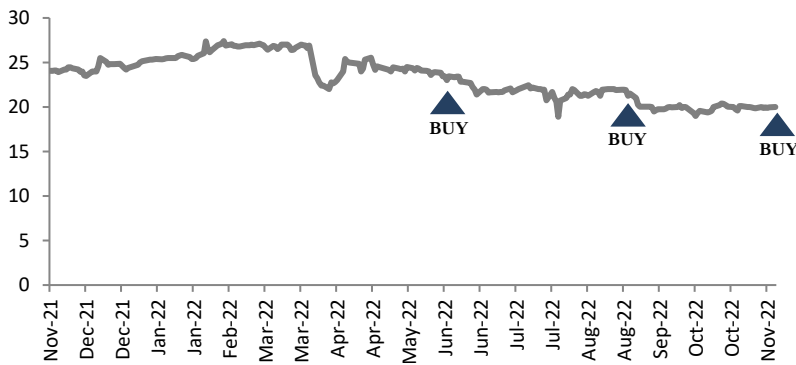
Valuation

Our valuation puts the target price of the stock at ₦30.38, representing an increase of 39.35% from the current price of ₦21.80. In arriving at the target price, we employed Dividend Discount Valuation Methodology. Consequently, we maintain a **STRONG BUY** recommendation on the stock of the bank.

Our valuation and forecasts considered several factors (both quantitative and qualitative) among which are; the previous financial reports of the bank, the current figures released by the bank, the performance of the bank in the banking industry and outlook from the bank’s management.

Our valuation puts the target price of the stock at ₦30.38, representing an increase of 39.35% from the current price of ₦21.80.

Fig. 8: Share Price History (Naira)



Source: NGX, PAC Research

Table 5: Statement of Profit or Loss, N'mn

	2020	2021	2022E	2023F
Gross Earnings	696,450	765,558	845,942	905,158
Change	5.16%	9.92%	10.50%	7.00%
Interest and Similar Income	420,813	427,597	499,106	534,043
Change	1.26%	1.61%	16.72%	7.00%
Interest and Similar Expenses	-121,131	-106,793	-122,662	131,248
Change	-18.45%	-11.84%	14.86%	7.00%
Net Interest Income	299,682	320,804	376,444	402,795
Change	12.23%	7.05%	17.34%	7.00%
Impairment Charge for credit losses	-39,534	-59,932	-67,675	-72,413
Change	64.51%	51.60%	12.92%	7.00%
Fees and Commission Income	79,332	103,958	131,121	140,299
Change	-20.75%	31.04%	26.13%	7.00%
Trade gains	121,678	167,483	186,107	199,135
Change	3.29%	37.64%	11.12%	7.00%
Personnel expenses	-79,520	-79,885	-88,824	-95,042
Change	2.13%	0.46%	11.19%	7.00%
Profit Before Taxation	255,861	280,374	298,617	318,615
Change	5.17%	9.58%	6.51%	6.70%
Taxation	-25,296	-35,816	-42,702	-45,562
Change	-26.57%	41.59%	19.23%	6.70%
Profit After Taxation	230,565	244,558	255,915	273,053
Change	10.40%	6.07%	4.64%	6.70%

Table 6: Statement of Financial Position, N'mn

	2020	2021	2022E	2023F
Cash and balances	1,591,768	1,488,363	1,813,986	1,904,685
Treasury bills	1,577,875	1,764,945	2,244,807	2,514,184
Assets pledged as collateral	298,530	392,594	453,496	507,916
Due from other banks	810,494	691,244	793,619	888,853
Derivative assets	44,496	56,187	87,298	97,774
Loans and advances	2,779,027	3,355,728	4,194,842	4,317,286
Investment securities	996,916	1,303,726	1,564,563	1,688,821
Deffered tax assets	5,786	12,013	11,860	13,850
Other assets	169,967	140,941	77,395	197,820
Property and equipment	190,170	176,182	185,216	186,764
Total Assets	8,481,272	9,447,843	11,337,412	12,697,901
Customer deposits	5,339,911	6,472,054	8,049,562	9,015,510
Derivative Liabilities	11,076	14,674	14,806	16,583
Other liabilities	703,292	487,432	623,558	698,385
On lending facilities	384,573	369,241	396,809	444,427
Borrowings	870,080	750,469	963,680	1,079,322
Debt securities issued	43,177	45,799	57,717	64,643
Total Liabilities	7,363,800	8,168,181	10,121,759	11,336,370
Net Assets	1,117,472	1,279,662	1,215,652	1,361,531
Total equity and liabilities	8,481,272	9,447,843	11,337,412	12,697,901

Tab. 7: Profitability Ratio

	2020	2021	2022E	2023F
Return on Equity	20.63%	19.11%	21.05%	20.05%
Return on Assets	2.72%	2.59%	2.26%	2.15%
Net int. income to Rev.	43.03%	41.90%	44.50%	44.50%
PBT margin	36.74%	36.62%	35.30%	35.20%
Net Profit Margin	33.11%	31.95%	30.25%	30.17%
ROCE	4.10%	4.07%	3.35%	3.19%

Tab. 8: Asset Utilisation

	2020	2021	2022E	2023F
Cash/Revenue	228.55%	194.42%	214.43%	210.43%
Revenue to total assets (x)	8.21%	8.10%	7.46%	7.13%
Interest Inc. / Total Assets	4.96%	4.53%	4.40%	4.21%
Other Income/ Total Assets	0.60%	0.40%	0.00%	0.00%
Rev. to total fixed assets	366.22%	382.76%	332.77%	317.92%
fixed asset turnover	27.31%	26.13%	30.05%	31.45%

Tab. 9: Liquidity Ratios

	2020	2021	2022E	2023F
Current ratio	1.15	1.16	1.12	1.12
Cash ratio	0.22	0.18	0.18	0.17
Interest Coverage ratio	2.11	2.63	2.43	2.43
Liquid Assets/Total Deposit	0.78	0.70	0.70	0.68
Loans & Adv./Total Deposit	0.52	0.52	0.52	0.48
Liquid Assets/Total Assets	0.49	0.48	0.50	0.48
Debt/net income	3.96	3.26	3.99	4.19
Debt to asset	0.11	0.08	0.09	0.09
Debt to equity	0.82	0.62	0.84	0.84
Total Liabilities / Total Asset	0.87	0.86	0.89	0.89
Cost to income ratio net interest margin AVERAGED	0.50	0.51	0.52	0.52
Total liabilities/equities	6.59	6.38	8.33	8.33

Tab. 10: Shareholders' Investment Ratios

	2020	2021	2022E	2023F
Earnings per share	7.34	7.79	8.15	8.70
DiV per share	3.00	3.10	3.20	3.30
NAVPS	35.59	40.76	38.72	43.37
Earnings yield	33.69%	35.73%	37.39%	39.89%

Tab. 11: Capital Adequacy Ratios

	2020	2021	2022E	2023F
Loans and Advances/Equity	2.49	2.62	3.45	3.17
Equity/Total Assets	0.13	0.14	0.11	0.11
Loan Loss Expense/ Equity	0.04	0.05	0.06	0.05

Source: Company's Annual Reports, PAC Research

Equity research methodology employed in this report

Views documented in this equity research report stem from conclusions reached through the use of multiple valuation methodologies, industry-wide knowledge, company specific information and our near to medium term expectations of industry and company performance, as well as market outlook. Our forecasts are based on a combination of top down and bottom up analysis, alongside historical trends in industry and company financials. Where appropriate, we factored in available forecasts and business direction provided by company management.

Our recommendation tends towards value investing. Therefore, our investment rank gauge—a customized scale we use to judge how well a firm under coverage has performed—is determined using major value parameters as well as relevant ratios and multiples computed with figures from the company's most recent financials.

The variables used to arrive at the company's investment rank cover a wide range of measures which characterize liquidity, operational efficiency, profitability, profit margins, growth, economic viability, gearing, relative valuation ratios, capital structure and management performance. Our investment recommendation is underpinned by the upside or downside potential of a stock under coverage. This potential is estimated by comparing the stock's current market price to its price target and fair value, on a percentage increase or decrease basis as summarized below:

Deviation from current price	Recommendation
>30%	STRONG BUY
10% to < 30%	BUY
-10% to < 10%	HOLD
<-10%	SELL

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