

## 2020 Results: Outstanding Performance Despite the Pandemic

### INVESTMENT SUMMARY

The year 2020 will be known as a pandemic year due to the outbreak of coronavirus which has not only claimed the lives of many people, but also affected businesses in many countries. However, COVID-19 did not have adverse impact on the performance of Zenith Bank in 2020. In line with our expectation, the gross earnings of the bank improved by 5.16% to ₦696.45 billion in FY'20 (vs. ₦662.25 billion in FY'19), driven by impressive performance across the board. The total interest income of the bank increased by 1.26% to ₦420.81 billion in FY'20 (vs. ₦415.56 billion in FY'19), as a result of higher average volume of risk assets. Due to higher foreign currency revaluation gain and treasury bills trading income, non-interest income rose by 8.45% to ₦251.75 billion in FY'20 (vs. ₦232.12 billion in FY'19). Impressively, the bank benefited from the lower interest rates (which reflected on cost of funds of 2.1% in FY'20 (FY'19: 3.0%)) as interest & similar expense fell by 18.45% to ₦121.13 billion (vs. ₦148.53 billion in FY'19). In line with our projection, the bank's loan impairment charge rose significantly by 64.51% to ₦39.53 billion in FY'20 (vs. ₦24.03 billion in FY'19), due to higher expected credit losses on loans & advances.

The profit before tax rose by 5.17% to ₦255.86 billion in FY'20 (vs. ₦243.29 billion in FY'19). However, a lower provision of ₦25.30 billion was made for tax in FY'20 (vs. ₦34.45 billion in FY'19) and as a result, profit after tax rose by 10.40% to ₦230.57 billion (vs. ₦208.84 billion in FY'19). Impressively, EPS rose to ₦7.34 in 2020, from ₦6.65 recorded in 2019. The bank proposed a final dividend of ₦2.70 per share (2019 Final dividend: ₦2.50) after the payment of ₦0.30 as interim dividend per share in 2020 (2019 interim dividend: ₦0.30), totalling ₦3.00 in FY'20 (FY'19: ₦2.80). Based on the recent figures released by the bank, we maintain a **BUY** rating on the stock at the current price of ₦26.30 as present forward estimate places the company share price at ₦30.29 (Previous TP: ₦28.12).

Fig. 1: Quarterly results highlights

	4Q2020	3Q2020	4Q2019	Q/q Δ	Y/y Δ
Gross Earnings (₦mn)	187,475	162,887	170,983	+15.10%	+9.65%
Net Int. Income (₦mn)	74,503	67,770	52,404	+9.94%	+42.17%
Net profit (₦mn)	71,250	55,489	58,120	+28.40%	+22.59%

Source: NSE, Bloomberg, PAC Research

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Price:

- Current	₦26.30
- Target	₦30.29
<b>Recommendation:</b>	<b>BUY</b>

\* As at Wednesday February 24, 2021

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	+6.05%/+32.49%
52-week range	₦28.50 - ₦10.70
30-day Average vol.	35,766,420
Shares Outstanding (mn)	31,396.49
Market Cap. (₦bn)	825.73
EPS (₦)	7.34
DPS (₦) - FY2020	3.00

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	FY'20	FY'19
Net Interest Margin	7.90%	8.20%
Net profit margin	33.11%	31.54%
Equity multiplier	7.59	6.74
Cash/ total Assets	18.77%	14.75%

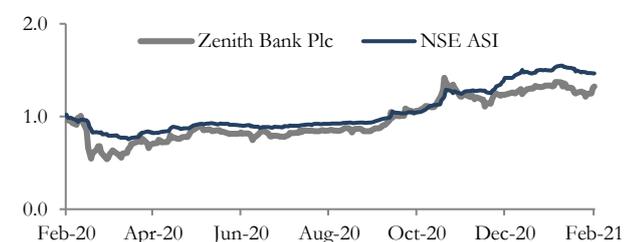
Source: NSE, Bloomberg, PAC Research

Fig. 4: Valuations

	FY2019	FY2020	FY2021F	FY2022F
P/E (x)	3.95	3.58	3.57	3.50
P/B (x)	0.88	0.74	0.66	0.62
Div Yield	10.65%	11.41%	11.41%	11.79%
Payout Ratio	42.09%	40.85%	40.77%	41.27%
EV/Revenue	1.52	1.77	1.76	1.74
Rev per share	21.09	22.18	22.85	23.65
ROE	22.17%	20.63%	18.40%	17.59%
ROA	3.29%	2.72%	2.56%	2.44%

Source: NSE, Bloomberg, PAC Research

Fig. 5: 52-Week Price Movement of ZENITH vs NSE ASI

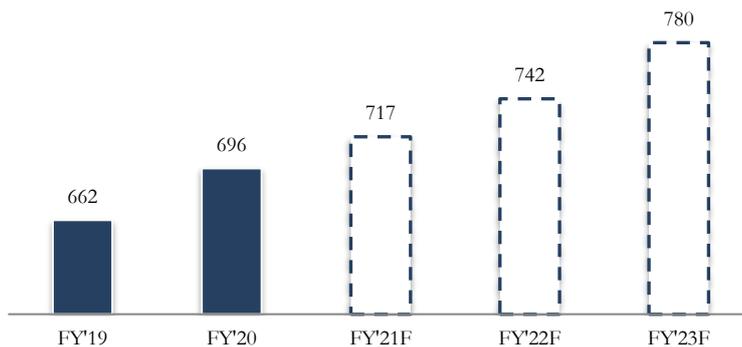


Source: Bloomberg, PAC Research

**Gross earnings improves by 5.16% year-on-year, driven by improved interest-income and non-interest income:** Despite a challenging macro-economic environment aggravated by the COVID 19 pandemic in 2020, Zenith Bank delivered impressive result as gross earnings increased by 5.16% to ₦696.45 billion (vs ₦662.25 billion recorded in 2019). The performance of the bank's top-line was mainly driven by the improved interest income and non-interest income during the period. The total interest income improved by 1.26% to ₦420.81 billion in FY'20 (₦415.56 billion reported in FY'19), mainly as a result of higher interest and similar income from loans & advances to customers and government & other bonds. In addition, the non-interest income rose significantly by 8.45% to ₦251.75 billion in FY'20 (vs. ₦232.12 billion in FY'19), driven by higher foreign currency revaluation gain and improved treasury bills trading income. Going forward, we may likely see moderate growth in the top-line and we expect this to be driven by interest income from loans and advances as we expect the bank to continue to benefit from the rising interest rates and regulatory requirement of 65% loan-to-deposit ratio.

*The performance of the bank's top-line was mainly driven by the improved interest income and non-interest income during the period.*

**Fig. 6: Gross Earnings – FY'19 – FY'23F (Billion NGN)**



Source: NSE, Bloomberg, PAC Research

**Interest income rises by 1.26% due to improvement in average volume of risk assets and fixed income securities:** In line with our forecast, Zenith bank benefited from the higher regulatory loan-to-deposit ratio of 65% as interest income from loans and advances to customers improved by 7.67% to ₦250.81 billion in FY'20 (vs. ₦232.95 billion in FY'19), even with reduced interest rates during the period. In addition, the bank may have also benefited from the long position taken in fixed income securities when yields were high as total interest income from the government and other bonds increased by 19.00% to ₦81.51 billion in FY'20 (vs. ₦68.50 billion in FY'19). However, there was a setback in interest income from treasury bills as it fell by 33.67% to ₦53.80 billion in FY'20 (vs. ₦81.11 billion reported in FY'19), due to reduction in interest rate during the period.

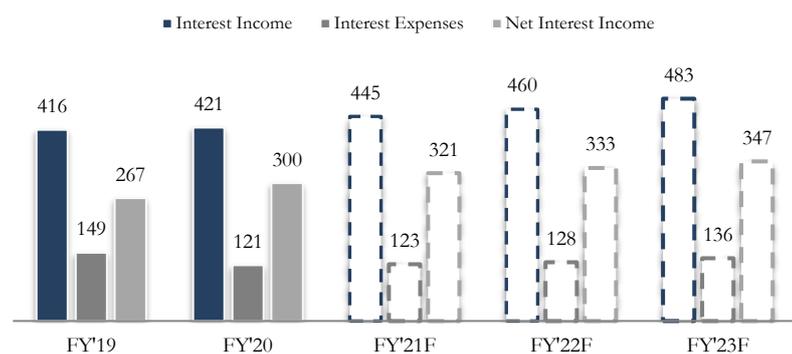
The improvement in interest income from loans & advances and government and & other bonds outweighed the setback recorded for interest income from treasury bills.

*...the bank may have also benefited from the long position taken in fixed income securities when yields were high as total interest income from the government and other bonds increased by 19.00%...*

Consequently, the total interest income improved by 1.26% to ₦420.81 billion in FY'20 (vs. ₦415.56 billion in FY'19). Going forward, we expect improvement in the bank's total interest income due to the rising yields in fixed income market.

Impressively, interest expenses declined significantly by 18.45% to ₦121.13 billion during the period (vs. ₦148.53 billion in FY'19), due to improvement in the cost of funds occasioned by the low interest environment during the period. The bank recorded a cost of funds of 2.10% in FY'20 (FY'19: 3.00%) and this translated to reduction of 38.15% and 41.03% in interest and similar expense on time deposit and borrowed funds & lease respectively. However, interest and similar expenses on current and savings accounts increased by 155.14% and 2.34% to ₦29.66 billion (FY'19: ₦11.62 billion) and ₦22.13 billion (FY'19: ₦21.63 billion) in FY'20 respectively. We may likely see a rise in the cost of funds in 2021 due to the rising interest rate in the country.

**Fig. 7: Interest Income and Interest Expenses: FY'19-FY'23F (Billion NGN)**



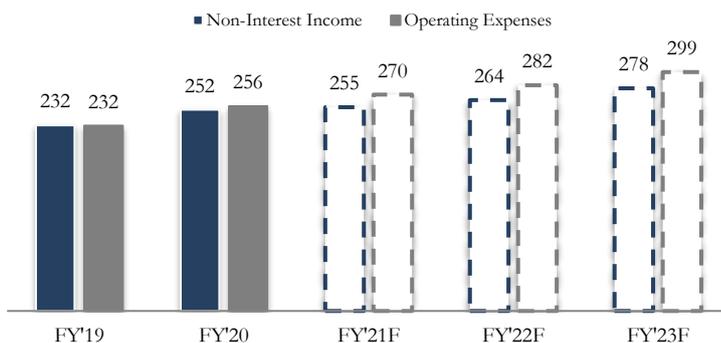
Source: NSE, Bloomberg, PAC Research,

**Trading income and foreign currency revaluation gain offsets the lower income from fee and commission as non-interest income improves by 8.45%:** In 2020, The regulatory cut to bank charges bite hard into income on fee and commission as it declined significantly by 9.98% to ₦103.22 billion (vs. ₦114.67 billion in 2019), driven by 36.30% and 36.41% fall in fees on electronic products and credit related fees respectively. However, trading income increased by 3.29% to ₦121.68 billion in FY'20 (₦117.80 billion in FY'19), mainly due to improved treasury bill trading income and higher bond trading income. Also, as a result of drop in the value of Naira in the FX market in 2020, foreign currency revaluation gain increased significantly by 276.44% to ₦43.44 billion in FY'20 (vs. ₦11.54 billion in FY'19). However, the improvement in trading income and foreign currency revaluation gain offset the setback in fee and commission income as total non-interest income rose by 8.45% to ₦251.75 billion in FY'20 (vs. ₦232.12 billion in FY'19).

The total operating expenses of the bank rose by 10.44% to ₦256.03 billion in FY'20 (vs. ₦231.83 billion in FY'19), due to higher depreciation of property and equipment, higher personnel expenses, higher deposit insurance premium, higher expenses on information technology, fuel and maintenance, among others. Impressively, the 10.44% increase in total operating expenses in 2020 is 531 bps lower than the inflation rate of 15.75% for the month of December 2020.

*..the 10.44% increase in total operating expenses in 2020 is 531 bps lower than the inflation rate of 15.75% for the month of December 2020*

Fig. 8: Non-Int. Income & Total Op. Expense: FY'19 - FY'23F (Billion NGN)

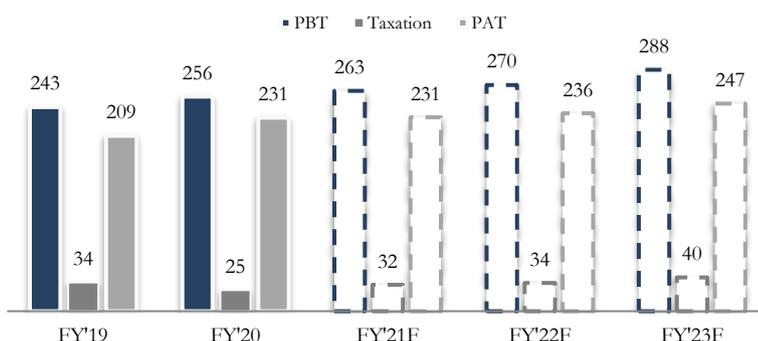


Source: NSE, Company's Results, PAC Research

**With impressive performance across board, PAT rises by 10.40% year-on-year:** In the year 2020, the bank reported an unimpressive figure for impairment charges as it increased significantly by 64.51% to ₦39.53 billion (vs. ₦24.03 billion in 2019), due to higher expected credit losses on loans and advances occasioned by the pandemic, which affected businesses in 2020. However, the impressive performance of the bank across the board offsets the higher impairment charge during the period as profit before tax increased by 5.17% to ₦255.86 billion in FY'20 (vs. ₦243.29 billion reported in FY'19). The bank made a lower provision of ₦25.30 billion for tax during the period (FY'19: ₦34.45 billion) and as a result, profit after tax increased by 10.40% to ₦230.57 billion in FY'20 (vs. ₦208.84 billion in FY'19). Impressively, EPS improved by 10.38% to ₦7.34, from ₦6.65 recorded in 2019.

*...the impressive performance of the bank across the board offsets the higher impairment charge during the period as profit before tax increased by 5.17%...*

Fig. 9: PBT, Taxation and PAT – FY'19 - FY'23F (Billion NGN)



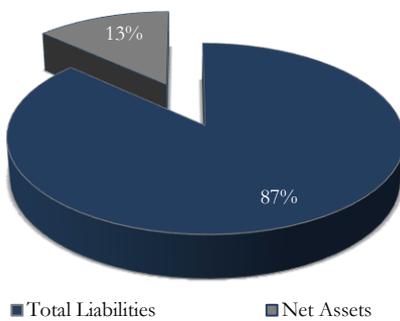
Source: NSE, Bloomberg, PAC Research

**With Solid and high quality capital position, the bank proposes final dividend payment of ₦2.70 per share:** The balance sheet of the bank remains strong and solid in the full year of 2019. This is evident in the strong liquidity ratio and capital adequacy ratio. Liquidity and Capital Adequacy Ratio (CAR) of the bank are well above industry requirements of 30% for liquidity ratio and 15% for capital adequacy ratio. The liquidity ratio was 62.5% while the capital adequacy ratio was 23.00% in 2020. However, the bank’s loan-to-deposit ratio of 64.5% in 2020 is slightly below the regulatory minimum requirement of 65.00%.

Mainly as a result of higher loans and advances and higher treasury bills, total assets increased by 33.63% to ₦8.48 trillion in FY’20 (vs. ₦6.35 trillion in FY’19). However, total liabilities increased significantly by 36.24% to ₦7.36 trillion in FY’20 (vs. ₦5.40 trillion in FY’19), mainly due to higher deposits from customers and borrowings. Consequently, net asset increased by 18.65% to ₦1.12 trillion in FY’20 (vs. ₦941.86 billion in FY’19) and this translated to a net asset per share of ₦35.59 (FY’19: ₦30.00). Impressively, the bank proposed a final dividend of ₦2.70 per share (2019 Final dividend: ₦2.50) after the payment of ₦0.30 as interim dividend per share in 2020 (2019 interim dividend: ₦0.30), totalling ₦3.00 in FY’20 (FY’19: ₦2.80).

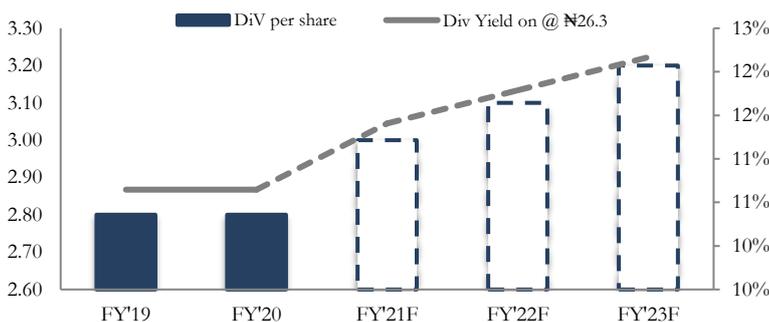
*...the bank proposed a final dividend of ₦2.70 per share (2019 Final dividend: ₦2.50) after the payment of ₦0.30 as interim dividend per share in 2020 (2019 interim dividend: ₦0.30), totalling ₦3.00 in FY’20 (FY’19: ₦2.80).*

Fig. 10: Total Liabilities Vs Net Asset in FY’20



Source: Company’s Presentation, PAC Research

Fig. 11: Dividend Per Share and Dividend Yield (FY’19-FY’23F)



Source: Company’s Presentation, PAC Research

### Valuation

Our valuation puts the target price of the stock at ₦30.29, representing an increase of 15.15% from the current price of ₦26.30. In arriving at the target price, we employed Dividend Discount Model and residual income valuation. Consequently, we maintain a **BUY** recommendation on the stock of the company. Our valuation and forecasts considered several factors (both quantitative and qualitative) among which are; the previous financial reports of the company, the current figures released by the company, the performance of the bank in the industry and outlook from the bank's management.

*Our valuation puts the target price of the stock at N30.29, representing an increase of 15.15% from the current price of N26.30. In*

Fig. 14: Share Price History (Naira)



Source: NSE, PAC Research

**Fig. 15: Statement of Profit or Loss, N'mn**

	2019	2020	2021F	2022F
Gross Earnings	662,251	717,344	742,451	779,573
Change	5.06%	8.32%	3.50%	5.00%
Interest and Similar Income	415,563	444,753	460,319	483,335
Change	-5.57%	7.02%	3.50%	5.00%
Interest and Similar Expenses	-148,532	-123,383	-127,701	136,425
Change	2.82%	-16.93%	3.50%	6.83%
Net Interest Income	267,031	321,370	332,618	346,910
Change	-9.66%	20.35%	3.50%	4.30%
Impairment Charge for credit losses	-24,032	-43,041	-44,547	-38,979
Change	30.81%	79.10%	3.50%	12.50%
Fees and Commission Income	100,106	89,668	94,291	100,565
Change	22.36%	-10.43%	5.16%	6.65%
Trade gains	117,798	136,295	139,581	146,560
Change	46.88%	15.70%	2.41%	5.00%
Personnel expenses	-77,858	-82,136	-85,011	-89,261
Change	13.57%	5.49%	3.50%	5.00%
Profit Before Taxation	243,294	262,548	269,510	287,662
Change	5.01%	7.91%	2.65%	6.74%
Taxation	-34,451	-31,506	-33,689	-40,273
Change	-9.96%	-8.55%	6.93%	19.54%
Profit After Taxation	208,843	231,042	235,821	247,390
Change	7.97%	10.63%	2.07%	4.91%

**Fig. 16: Statement of Financial Position, N'mn**

	2019	2020	2021F	2022F
Cash and balances	936,278	1,695,233	1,810,509	1,939,055
Treasury bills	991,393	1,680,437	1,794,707	1,922,131
Assets pledged as collateral	431,728	317,934	339,554	363,662
Due from other banks	707,103	863,176	921,872	987,325
Derivative assets	92,722	47,388	50,611	54,204
Loans and advances	2,305,565	2,959,664	3,160,921	3,385,346
Investment securities	591,097	1,061,716	1,133,912	1,214,420
Deferred tax assets	11,860	11,860	6,162	6,581
Other assets	77,395	77,395	181,015	193,324
Property and equipment	185,216	185,216	202,531	216,303
Total Assets	6,346,854	9,032,555	9,646,768	10,331,689
Customer deposits	4,262,289	5,621,862	6,004,149	6,430,443
Derivative Liabilities	14,762	11,796	12,598	13,493
Other liabilities	363,764	749,006	799,938	856,734
On lending facilities	392,871	409,570	437,421	468,478
Borrowings	322,479	926,635	989,646	1,059,911
Debt securities issued	39,092	45,984	49,110	52,597
Total Liabilities	5,404,993	7,777,030	8,305,868	8,895,584
Net Assets	941,861	1,255,525	1,340,901	1,436,105
Total equity and liabilities	6,346,854	9,032,555	9,646,768	10,331,689

**Fig. 17: Profitability Ratio**

	2019	2020	2021F	2022F
Return on Equity	22.17%	18.40%	17.59%	17.23%
Return on Assets	3.29%	2.56%	2.44%	2.39%
Net int. income to Rev.	40.32%	44.80%	44.80%	44.50%
PBT margin	36.74%	36.60%	36.30%	36.90%
Net Profit Margin	31.54%	32.21%	31.76%	31.73%
ROCE	5.45%	4.03%	3.87%	3.86%

**Fig. 18: Asset Utilisation**

	2019	2020	2021F	2022F
Cash/Revenue	141.38%	236.32%	243.86%	248.73%
Revenue to total assets (x)	10.43%	7.94%	7.70%	7.55%
Interest Inc. / Total Assets	6.55%	4.92%	4.77%	4.68%
Other Income/ Total Assets	0.22%	0.32%	0.31%	0.30%
Rev. to total fixed assets	357.56%	354.19%	343.25%	336.52%
fixed asset turnover	27.97%	28.23%	29.13%	29.72%

**Fig. 19: Liquidity Ratios**

	2019	2020	2021F	2022F
Current ratio	1.17	1.16	1.16	1.16
Cash ratio	0.17	0.22	0.22	0.22
Interest Coverage ratio	1.64	2.13	2.11	2.11
Liquid Assets/Total Deposit	0.59	0.79	0.79	0.79
Loans & Adv./Total Deposit	0.54	0.53	0.53	0.53
Liquid Assets/Total Assets	0.40	0.49	0.49	0.49
Debt/net income	1.73	4.21	4.40	4.50
Debt to asset	0.06	0.11	0.11	0.11
Debt to equity	0.38	0.77	0.77	0.77
Total Liabilities / Total Asset	0.85	0.86	0.86	0.86
Cost to income ratio net interest margin AVERAGED	0.49	0.51	0.51	0.51
Total liabilities/equities	5.74	6.19	6.19	6.19

**Fig. 20: Shareholders' Investment Ratios**

	2019	2020	2021F	2022F
Earnings per share	6.65	7.36	7.51	7.88
DiV per share	2.80	3.00	3.10	3.20
NAVPS	30.00	39.99	42.71	45.74
Earnings yield	25.29%	27.98%	28.56%	29.96%

**Fig. 21: Capital Adequacy Ratios**

	2019	2020	2021F	2022F
Loans and Advances/Equity	2.45	2.36	2.36	2.36
Equity/Total Assets	0.15	0.14	0.14	0.14
Loan Loss Expense/ Equity	0.03	0.03	0.03	0.03

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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