

Zenith Bank Plc.

First Glance: Decline in Opex Supported 42.57% q/q Growth in PAT, Despite Lower Funding Income and Non-Interest Revenue.

Zenith Bank Plc (ZENITHBANK) published Q3-2017 result this afternoon, reporting declines across most line items – gross earnings declined 35.19% q/q and 8.89% y/y – following higher than expected contraction in interest income (-30.96% q/q and +4.54% y/y) and a steep decline in non-interest revenue (42.07% q/q and 16.29% y/y). ZENITHBANK's annualized EPS rose 41.32% to N1.71, above consensus estimate of N1.08.

The q/q decline in interest income (28.87% below our estimate) was on the back of lower interest on loans and advances to customers (-37.455 q/q and -18.27% y/y), interest income on treasury bills (-22.83% q/q), and bonds (-4.23% q/q and -22.95% y/y), resulting in a 134 bps y/y contraction in annualized asset yield to 10.04% – a development we attribute to the negative base effect of the asset re-pricing and translation impact of FCY interest income which supported funding income in the previous year. On the other hand, interest expense declined 10.78% y/y and 51.19% q/q, broadly reflecting a significant decline on interest on time deposits (74.29% q/q and 41.79% q/q), resulting in 37 bps y/y decline in annualized cost of funds to 4.00%. Overall, annualized NIM contracted 96 bps to 6.34%.

Also, the relative stability of the naira – which limited the legroom for significant revaluation gains such as those reported last year – largely accounted for the huge drop in NIR. The decline was further exacerbated by a N17.63 billion foreign exchange trading loss in Q3-17, which masked the surge in treasury bill trading income (+182.96% q/q and 1151.07% y/y).

Over 9M-17, asset quality deterioration persists, with NPL ratio rising 200 bps y/y to 4.20% (albeit below the 4.30% in H1-17), while additional provisioning of N4.67 billion in Q3-17 further pushed cost of risk 140 bps higher to 2.70%, following specific provision on bilateral exposure to Etisalat (now 9 Mobile) and collective allowance for impairment on exposures to the general commerce, transportation, oil & gas, and power sectors.

On the positive, total opex declined 16.51% y/y and 34.41% q/q (15.29% below our estimate) in Q3-17, following moderations in personnel expenses (-13.72% y/y and -2.85% q/q) and operating expenses (-21.19% y/y and -47.75% q/q), the cumulative impact of which offset the 20.31% y/y and 7.80% q/q increase in depreciation and amortization.

Specifically, over 9M-17, ZENITH's gross earnings is up 39.68% (supported by 26.6% and 79% increase in interest and non-interest incomes) while PBT and PAT are both ahead by 25.79% and 29.14% respectively. Accordingly, EPS is ahead of last year's by 29.14% to N4.12.

While acknowledging the strong performance over 9M-17, the contraction across lines in Q3-17 would likely drive downward review of consensus 2017 estimates. Based on our last TP of N27.19, at 3.58% premium to the current market price of N26.25, we have a HOLD recommendation on the stock. Our estimates are under review.

HOLD

Target Price (N)*	27.19
Current Price (N)	26.25
Implied Return (%)	3.58

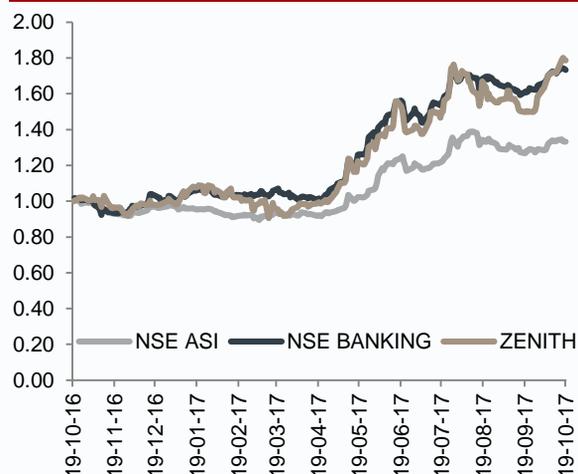
Company Data

NSE Code	ZENITHBANK
Bloomberg Code	ZENITHBA:NL
Reuters Code	ZENITHB.LG
Sector	FINANCIAL SERVICES
Market Cap. (N'bn)	824.15
Free Float (%)	90.45

Ratios	9M-2017	9M-2016	2016FY
Assets Yield	12.2%	11.5%	11.79%
Cost of funds	5.4%	3.8%	4.2%
Net Interest Margin	7.2%	7.6%	7.4%
Cost of Risk	2.7%	1.3%	1.4%
NPL/Total Loans	4.2%	2.2%	3.0%
CAR	22.2%	19.0%	23.0%
Liquidity Ratio	61.1%	55.2%	59.6%
Cost to Income	52.9%	53.8%	52.7%
Loan to Deposit	64.0%	72.3%	67.8%
cCoverage Ratio	110.3%	126.4%	100.1%

*Under Review **Trailing 12m

Price movement (ZENITHBANK vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

Highlight (N'Mn)	9M-2017	9M-2016	Y/Y	Cordros' Estimate	Variance	Q3-2017	Q2-2017	Q/Q	Cordros' Estimate	Variance
Gross Earnings	531,266	380,352	39.68%	486,313	9.24%	150,826	232,704	-35.19%	172,658	150,826
Interest Income	361,789	285,674	26.64%	377,701	-4.21%	99,532	144,165	-30.96%	139,927	99,532
Interest Expense	(160,297)	(95,857)	67.23%	(166,066)	-3.47%	(37,002)	(75,807)	-51.19%	(54,442)	(37,002)
Net Interest Income	201,492	189,817	6.15%	211,635	-4.79%	62,530	68,358	-8.53%	85,485	62,530
NIR	169,477	94,678	79.00%	108,612	56.04%	51,294	88,539	-42.07%	32,731	51,294
Operating Income	370,969	284,495	30.40%	320,247	15.84%	113,824	156,897	-27.45%	118,216	113,824
Provisions	(47,053)	(21,858)	115.27%	(42,619)	10.40%	(4,655)	(34,512)	-86.51%	(17,085)	(4,655)
OPEX	(171,364)	(141,362)	21.22%	(154,552)	10.88%	(48,800)	(74,402)	-34.41%	(57,607)	(48,800)
PBT	152,552	121,275	25.79%	123,076	23.95%	60,369	47,983	25.81%	43,524	60,369
Taxation	(23,317)	(21,201)	9.98%	(20,358)	14.54%	(6,451)	(10,165)	-36.54%	(9,666)	(6,451)
PAT	129,235	100,074	29.14%	102,719	25.81%	53,918	37,818	42.57%	33,858	53,918

Disclosures.

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