

FSDH Banking Sector Expectations: Post COVID-19 to weigh on Nigerian Banks

Post COVID-19 Economic Slowdown to Weigh on Nigerian Banks

The ravaging impact of the covid-19 pandemic has been felt across most sectors of the Nigerian economy in 2020. The recently published May PMI data from the Central Bank of Nigeria (CBN) puts Manufacturing & Non-Manufacturing PMI at 42.2 and 25.3 respectively signifying most sectors are currently in deep contraction. It is expected that while economic activities would continue to recover, we see business and consumer confidence remaining subdued through 2020 with a second wave of the covid-19 pandemic becoming an increasing possibility. We believe the banking sector will not remain as resilient in its performance. Thus, we highlight our expectations for the banking sector:

- **Loan growth to be subdued in 2020**

We expect the impact of slower economic activity and weak business confidence to weaken demand for loans by businesses as working capital needs decline while investment in capital expenditure softens. Thus, we expect loan growth for Nigeria commercial banks to be subdued in 2020.

- **Impairment charge to climb on accelerating default rate**

We anticipate banks would book increased impairment charges in 2020. This is premised on 2 key factors; i) Increased credit growth in 2019 as banks strove to meet CBN's minimum LDR requirement ii) Vulnerabilities in oil and non-oil economic activities could accelerate default rates among borrowers with FCY loans default rate expected to pick up.

- **Asset quality to remain fairly stable**

Nevertheless, we remain fairly comfortable on asset quality for most Nigerian banks. We do not expect any significant spike in NPLs as the CBN has given banks regulatory headroom to restructure loans in vulnerable sectors. Also, we remain comfortable with CAR levels of most Nigerian banks.

- **Interest income would be pressured**

At the recently concluded MPC meeting, the CBN confirmed its shift towards a dovish stance on monetary policy. Against this backdrop, we expect interest rates would be pressured for the rest of the year. This would have a positive impact on Cost of Funds as deposit rates decline while Asset Yield would be negatively affected. In addition, we expect the rate of decline in Asset Yield to be faster than the decline Cost of Funds due to; i) Considerably weaker yields on government securities ii) Weaker loan demand iii) Increased competition for quality borrowers amidst strive to comply with CBN's minimum LDR requirement. Overall, this implies Net Interest Margin for banks would be lower in 2020 and consequently would impact Net Interest income.

- **Non-Interest income the bright light**

Amidst the negatives, we expect Non-Interest income to be buoyed by higher E-Banking & Mobile Transactions. In addition, fixed income instruments have been repriced higher on lower yields in the fixed income market. Thus, we expect banks would book significantly improved trading income for the rest of the year. This would further buoy Non-Interest income.

- **Top picks remain stable & quality names**

Overall, we advise investors who maintain interest in banking stocks to buy banks with i) Strong Non-Interest Income generation ii) Quality history of Trading & FX Income iii) Quality risk management and iv) History of quality dividend payment. Considering the above metrics, we retain interest in our quality names and they include; **GTBank, Zenith Bank, UBA, and Stanbic IBTC.**

FSDH TOP PICKS¹

	Current Price	52-Week High	52-Week Low	All Time High	All-Time Low	Current P/E	5-Year Average P/E	Current P/B	5-Year Average P/B	Dividend Yield
NGSEINDEX Index	25,221.29	31,420.68	20,651.59	n/a	n/a	7.8x	n/a	1.1x	n/a	7.8%
ZENITHBA NL Equity	17.90	23.00	10.70	34.20	5.30	2.7x	3.8x	0.6x	0.8x	15.6%
UBA NL Equity	7.20	9.25	4.40	21.55	1.25	2.8x	3.0x	0.4x	0.5x	13.9%
Access NL Equity	7.35	12.00	5.30	21.58	1.40	2.6x	2.9x	0.4x	0.5x	9.2%
STANBIC NL Equity	35.80	43.00	23.50	53.25	4.27	5.0x	7.7x	1.2x	1.7x	9.1%
UACN NL Equity	9.00	11.15	4.30	69.87	1.96	2.8x	10.3x	0.5x	0.6x	1.1%
NESTLE NL Equity	995.00	1,469.90	750.00	1,645.00	30.13	17.9x	39.8x	13.9x	23.0x	6.4%
FLOURMIL NL Equity	21.00	24.00	12.10	96.05	5.68	16.3x	9.1x	0.6x	0.7x	5.7%
DANGSUGA NL Equity	14.00	16.60	8.50	46.67	3.13	8.3x	6.5x	1.7x	1.7x	7.9%
OKOMUOIL NL Equity	64.40	74.00	40.15	94.70	1.43	9.4x	8.8x	2.0x	2.3x	3.1%
MTNN NL Equity	115.00	146.80	90.00	159.30	90.00	11.4x	n/a	12.0x	n/a	4.2%

¹ Source: Company Financials, FSDH Research, May 30th,2020