2021 Banking Sector Outlook:
Nigerian Banks Face Struggles On Many Fronts

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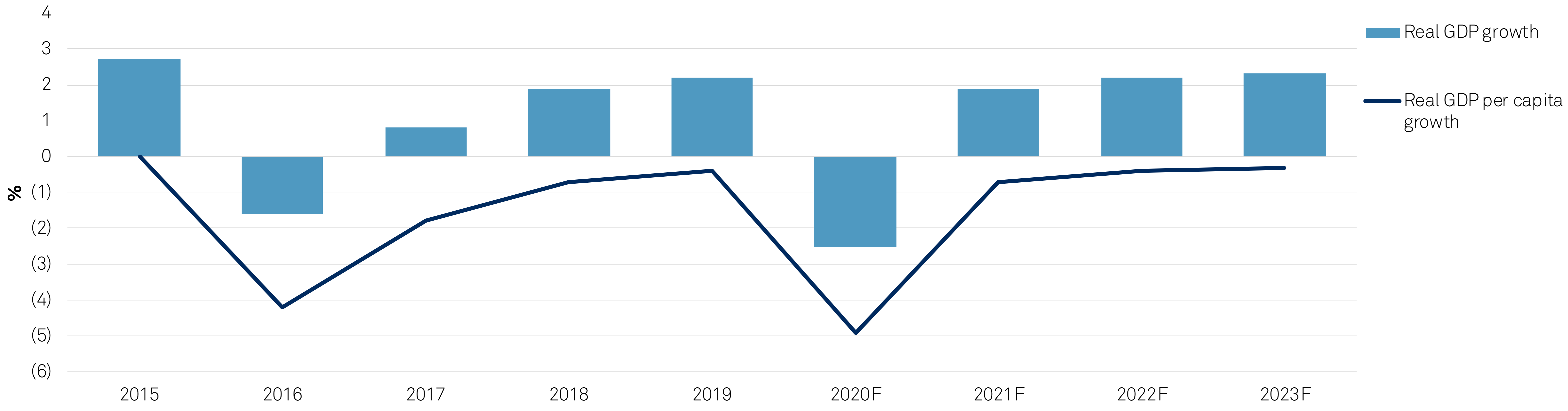
Key Takeaways

- Nigerian banks will grow slower in 2021 on the back of a subdued economy, despite the Central Bank of Nigeria's introduction of a minimum ratio of loans to deposits in 2019. We expect GDP growth will average about 2% a year through 2023 after a contraction that we estimate at about 2.5% in 2020.
- Economic setbacks will persist despite more sustained oil prices that we now project at $60 a barrel in 2021 and 2022 and because the vaccine rollout is in early stages. We also expect the Nigerian naira to weaken further to around NGN430/$1 in 2021 because of low foreign exchange inflows.
- We expect that last year's economic fundamentals will constrain Nigerian banks' risk appetite, leading to private-sector credit growth of about 5% in 2021.
- Earnings growth is likely to slow down because of higher credit impairments in 2020 and 2021 and the AMCON levy (to fund bank cleanups). Meanwhile, we expect the banking sector's credit losses will hover around 2.5%, and nonperforming loans to rise to 12% of total loans.
- While most of our rated banks operate with strong regulatory capital buffers, others might need a capital injection if the naira depreciates beyond our expectations.
- External debt of the banking sector will remain manageable, while U.S. dollar supply remains tight. Most Nigerian banks are largely funded by customer deposits, but lower-tier banks rely on wholesale funding.

An Economic Recovery May Prove To Be Elusive

- Setbacks from partial economic lockdowns, lower oil prices, and OPEC production quotas led to negative economic growth.
- The government will nevertheless attempt to increase oil production on the back of a new petroleum bill and shore up its foreign exchange reserves to address the economy's U.S. dollar shortage.
- Signs of recovery are still elusive; economic growth has been below the 5% historical average prior to the 2016 crisis.

Nigeria's Economy Is Vulnerable To External Shocks



F--Forecast. Source: S&P Global Ratings.

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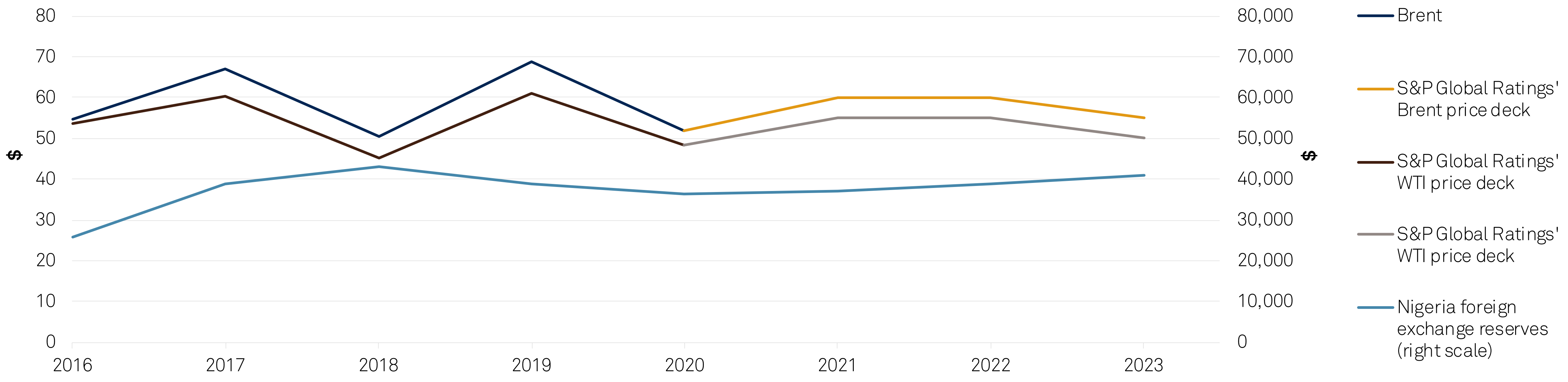
Nigeria Foreign Exchange Reserves Are Tied To Oil Prices

- The Central Bank of Nigeria (CBN) has been managing its foreign exchange reserves tightly because of lower oil receipts. Oil companies are selling their foreign exchange directly to CBN.
- CBN lowered its official exchange rate twice: in March by about 15% and August 2020 by about 5%.
- Foreign exchange reserves for 2021 are likely to remain broadly flat compared with 2020, at about $37 billion.

Nigeria's Foreign Exchange Reserves Will Follow The Same Path As Oil Prices



WTI--West Texas Intermediate. Source: S&P Global Ratings.

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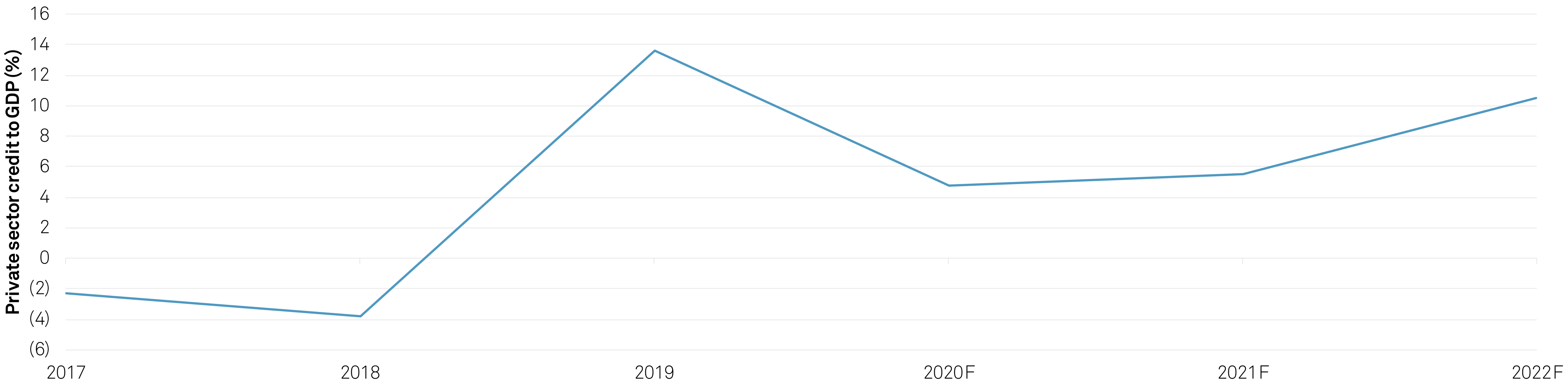
Lending Growth Will Remain Subdued

- We forecast subdued credit growth to the private sector of about 4%-6% in 2020 and 2021, after a strong 13.9% rebound in 2019, as the foreign exchange market and consumer demand stabilizes.
- The attractiveness of the upstream oil sector will depend on oil price trends. Legacy downstream issues will persist, but the removal of subsidies could help in the event of a recovery.
- Banks will likely focus on blue chips operating across the manufacturing, trade, and telecommunications sectors.

Loan Growth Will Likely Slow Despite A Rebound In 2019

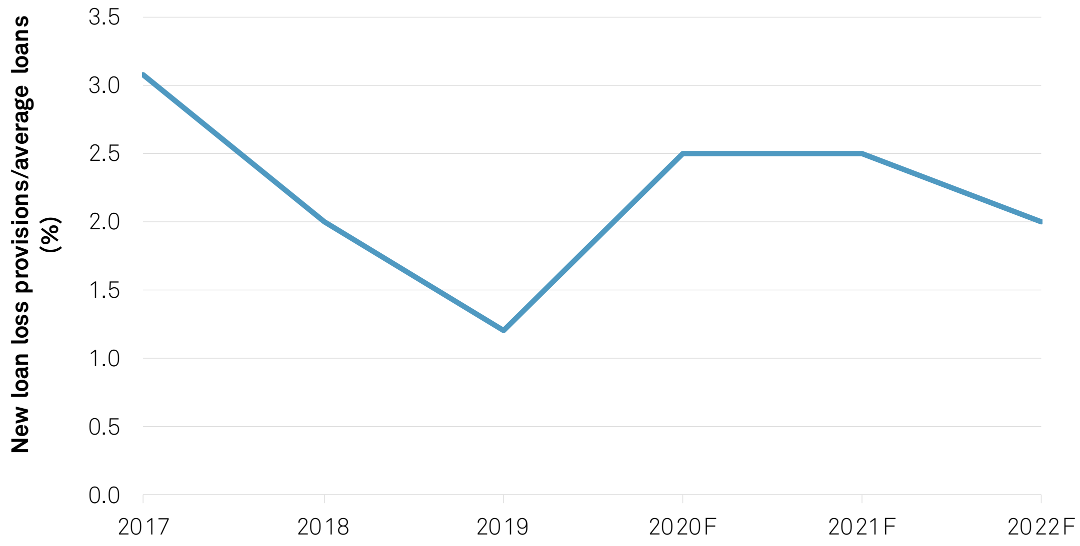


F--Forecast. Source: S&P Global Ratings.

Credit Risk Is Rising From An Already High Level

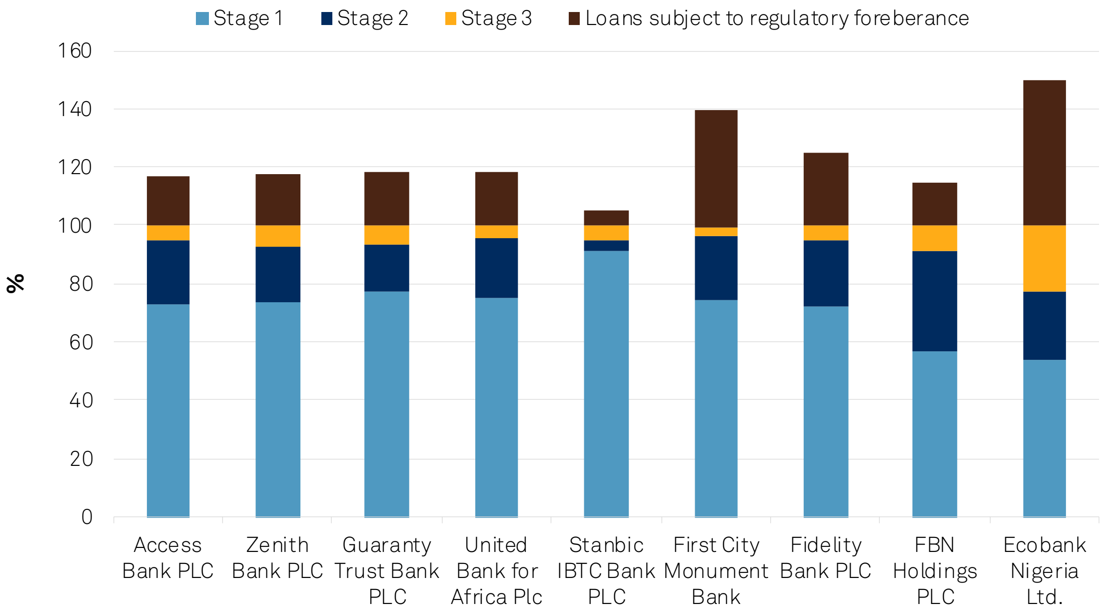
- Regulatory forbearance measures--on an average 23% of loans for rated banks--will likely delay recognition of NPLs, which we expect will double to 12% in 2021 from our estimate of 6% in 2019. Restructured loans could reach 25% of total loans.
- The share of foreign currency loans will remain high at about 50% of total loans on the back of a weakening naira. These loans are largely backed by receivables in the same currency, but not all exposures are hedged. In addition, single-name and sector concentration of loans are high with banks serving the same corporates.

We Forecast Banking Sector Credit Losses To Rise



F--Forecast. Source: S&P Global Ratings.

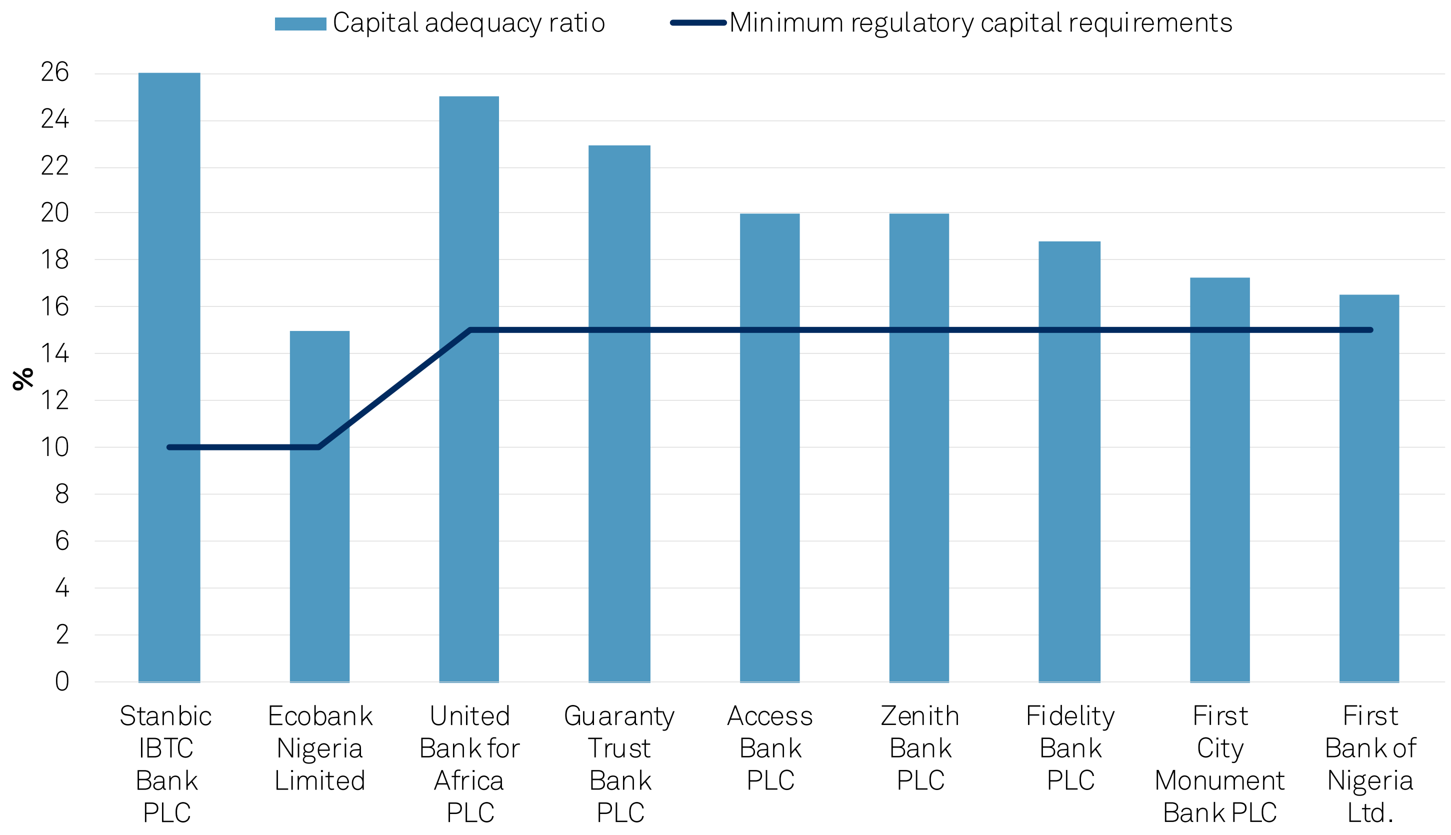
Loan Book Staging Of Nigerian Banks At End-June 2020



Source: S&P Global Ratings.

After Taking A Hit In 2020, Profitability Will Gradually Improve

Most Rated Nigerian Banks Have Strong Regulatory Capital Buffers



CAR--Capital adequacy ratio. Requirements are national minimum. Source: Company Financials. Data at June 30, 2020.

- We expect banks' profitability will weaken in 2020 and 2021, with return on assets declining to 1.5%-1.8% because of higher impairment charges and lower interest rates.
- We see the COVID-19 crisis as an earnings event for most banks we rate. We do not discount capital events for lower-tier banks, especially in case of sharp local currency depreciation.
- Raising equity will remain difficult in 2021, but banks could resort to raising tier 2 debt to support their regulatory capital.
- Alternatively, banks operating only in Nigeria have the option of converting their international banking license into a national license that calls for a lower minimum capital adequacy ratio.

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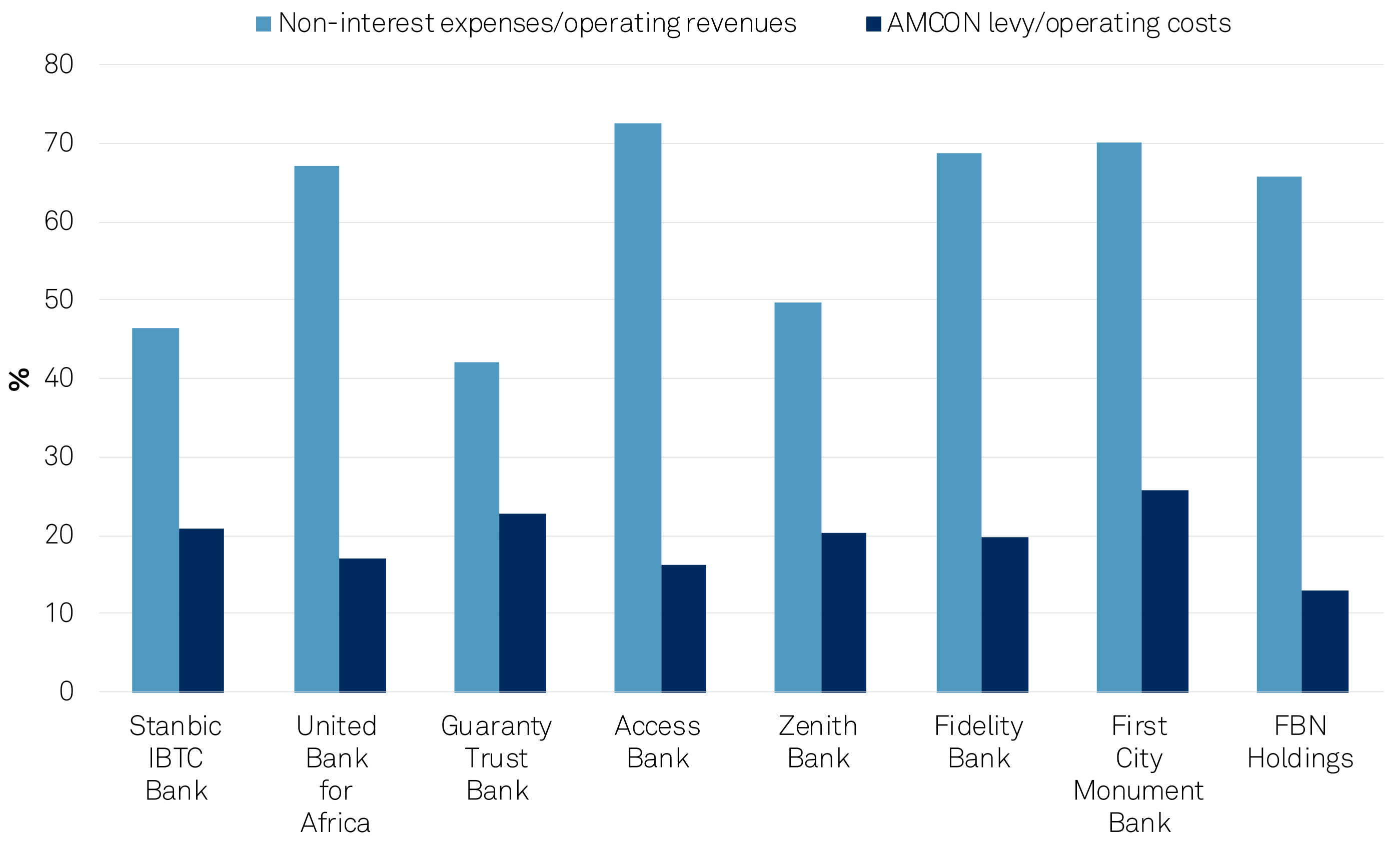
AMCON Levy Will Weigh On Banks' Profitability

AMCON Levy Undermines Nigerian Banks' Efficiency



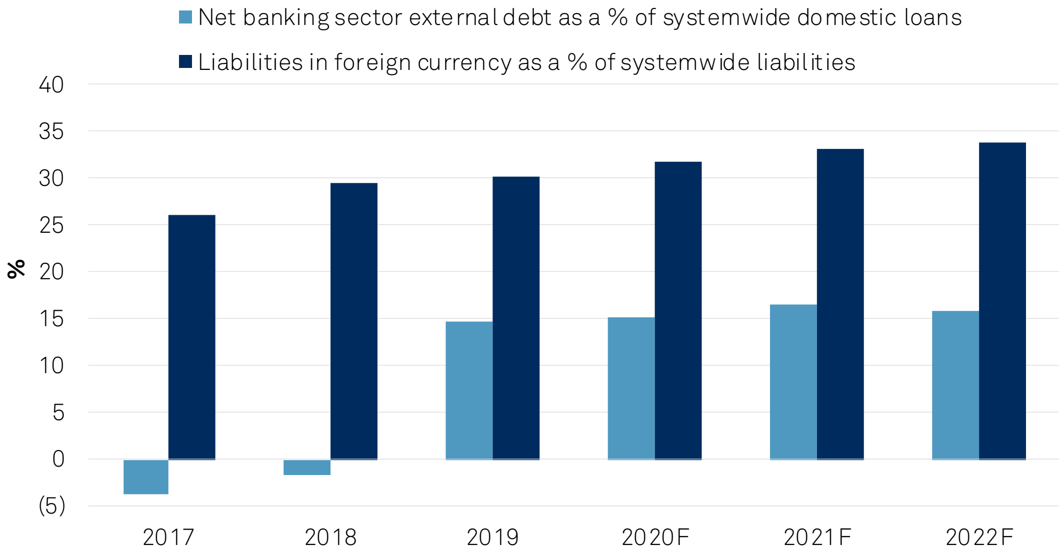
Source: Company Financials. Data at June 30, 2020.

- The CBN created the Asset Management Company Of Nigeria (AMCON) in 2010 to help clean up banks' bad loans over a 10-year period.
- Loan recoveries have been weak, so AMCON is largely relying on bank levies to pay back AMCON bonds issued to purchase problem assets.
- While the AMCON window is closed, the banks will continue to pay levies calculated on the size of their asset base over the medium term.
- These levies account for about 20% of banks' operating costs and weigh on their profitability and efficiency metrics.

Pressure On U.S. Dollar Balance Sheets Will Persist In 2021

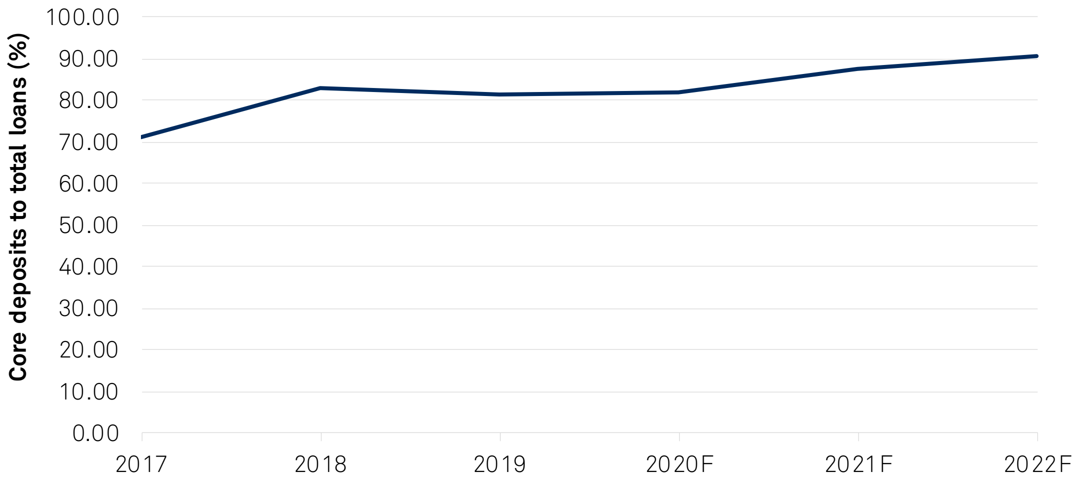
- Banks are largely funded by low-cost deposits, with lower-tier banks relying more on professional money managers, whose deposits are more confidence sensitive in time of crisis.
- The CBN is actively managing liquidity, using a minimum cash reserve requirement of 27.5% and loan to deposit of 65%.
- While foreign currency deposits have been stable, accounting for 25% of total deposits in 2019, the U.S. dollar shortage in the system is adding to the constraints on banks' liquidity.
- Refinancing risk has stabilized at more manageable levels of about 15% of systemwide loans.

Foreign Currency Liabilities To Remain Manageable



Source: S&P Global Ratings.

Stable Funding Profiles Could Improve Further

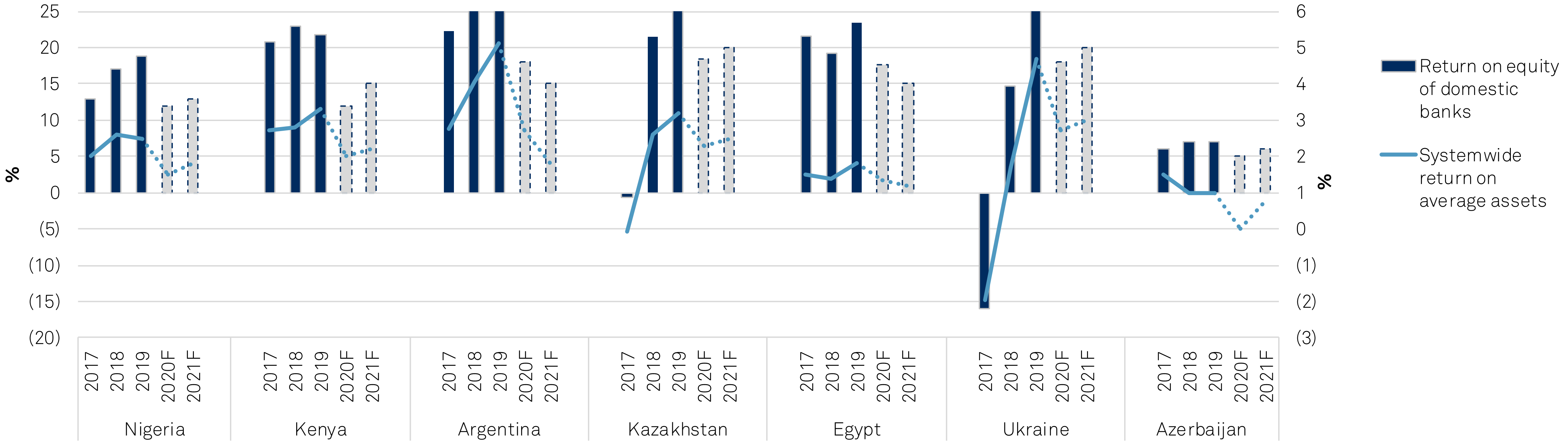


Source: S&P Global Ratings.

Nigerian Banks Remain Profitable Despite Soft Earnings

- The earnings decline at Nigerian banks is in line with peers'.
- We expect a gradual recovery after 2022, with returns on equity and assets rising to pre-pandemic levels.

Nigerian Banks' Profitability Drop Is In Line With Peers'

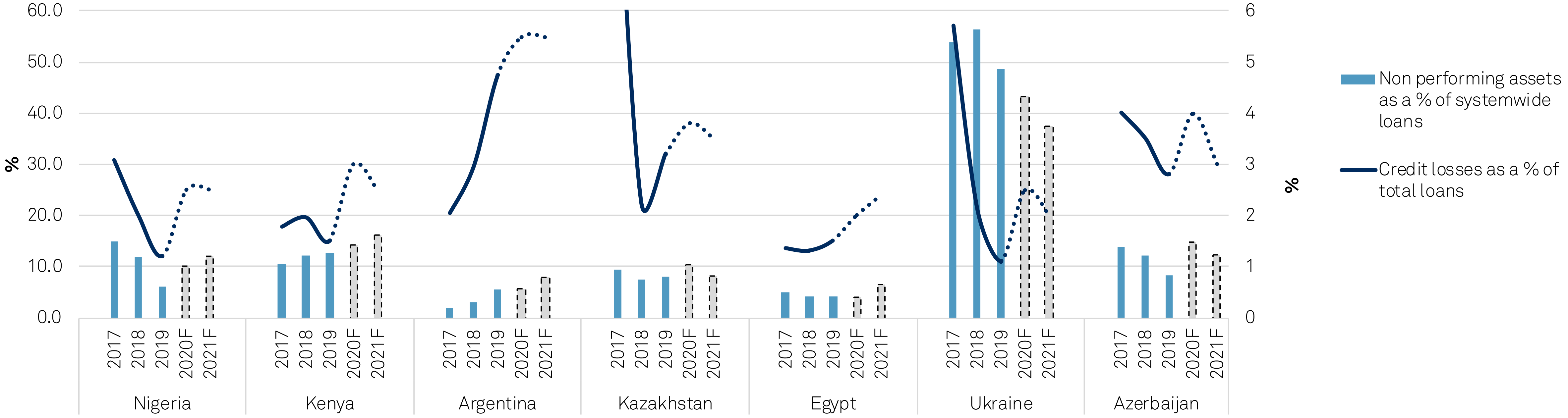


F--Forecast. Source: S&P Global Ratings.

Asset Quality Metrics Are Broadly In Line With Peers'

- Recognition of NPLs will take some time on the back of regulatory forbearance measures introduced in 2020 to lessen the impact of the pandemic.
- Credit losses compare well with peers' and are unlikely to rise to the same levels following the 2016 oil price shock.

Nigerian Banks' Asset Quality Compares Adequately To Peers'



Source: S&P Global Ratings.

Sovereign Ratings Constrain The Ratings On Top-Tier Nigerian Banks

- Top-tier Nigerian banks' stand-alone creditworthiness remains at 'b', but their credit ratings are constrained by the 'B-' sovereign rating.
- The stand-alone ratings reflect our expectation that banks' financial performance will remain resilient to the initial earnings shock stemming from the 2020 economic fallout.
- We have a stable outlook on the ratings on all the banks we rate in Nigeria, which largely reflect the stable outlook on the sovereign.
- Banks' ratings will move in tandem with the sovereign ratings, but an upgrade is unlikely in the next 12 months, unless Nigeria' economic performance is stronger than our expectations or if external financing pressures are contained. We could lower the ratings on banks if we see increasing risk to Nigeria's capacity to repay commercial obligations.

Nigerian Banks: Ratings And Outlooks

	SACP	ICR	National scale rating	Outlook
Access Bank PLC	b	B-/B	ngBBB/--/ngA-2	Stable
Ecobank Nigeria Ltd.		B-/B	--	Stable
Fidelity Bank PLC	b-	B-/B	ngBBB-/--/ngA-3	Stable
First Bank of Nigeria Ltd.	b-	B-/B	ngBBB-/--/ngA-3	Stable
First City Monument Bank Ltd.	b-	B-/B	ngBBB-/--/ngA-3	Stable
Guaranty Trust Bank PLC	b	B-/B	ngBBB/--/ngA-2	Stable
Stanbic IBTC Bank PLC	b-	B-/B	ngBBB/--/ngA-2	Stable
United Bank for Africa Plc	b	B-/B	ngBBB/--/ngA-2	Stable
Zenith Bank PLC	b	B-/B	ngBBB/--/ngA-2	Stable

SACP--Stand-alone credit profile. ICR--Issuer credit rating. Data as of Feb. 17, 2021. Source: S&P Global Ratings.

Related Research

- S&P Global Ratings Revises Oil And AECO Natural Gas Price Assumptions And Introduces Dutch Title Transfer Facility Assumption, March 8, 2021
- Nigeria, Feb. 15, 2021
- Banking Industry Country Risk Assessment: Nigeria, Nov. 30, 2020
- S&P Global Ratings Revises Oil And Natural Gas Price Assumptions, Sept. 16, 2020
- Central Banks In Africa Are Guiding Banks Through COVID-19 Economic Fallout, July 22, 2020
- Various Rating Actions On Nigerian Banks Following Sovereign Downgrade; Outlooks Stable, March 3, 2020
- Nigeria Long-Term Rating Lowered To 'B-' On Weakening External Position Tied To Sharp Fall In Oil Prices; Outlook Stable, March 26, 2020

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