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## Research Update:

# First Bank of Nigeria Outlook Revised To Stable; 'B-/B' Ratings Affirmed; National Scale Rating Raised To 'ngBB+'

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## Research Update:

# First Bank of Nigeria Outlook Revised To Stable; 'B-/B' Ratings Affirmed; National Scale Rating Raised To 'ngBB+'

## Overview

- First Bank of Nigeria Ltd.'s regulatory capital has improved and the risk of breaching regulatory requirements has thus diminished, while the bank's funding and liquidity remain a credit strength.
- Although asset quality remains a weakness, the steadying of the oil price and new management's efforts are helping to stabilize it.
- We are therefore revising the outlook on FirstBank to stable from negative and affirming our global scale ratings at 'B-/B'. In addition, we are raising the long-term national scale rating on FirstBank to 'ngBB+' from 'ngBB'.
- The stable outlook reflects our view that the bank will maintain its regulatory capital adequacy ratio (CAR) above the minimum requirement, continue to stabilize asset quality, although still at weak levels, and maintain its above average funding and adequate liquidity over the next 12 months.

## Rating Action

On June 21, 2017, S&P Global Ratings revised its outlook on Nigeria-based First Bank of Nigeria Ltd. (FirstBank) to stable from negative. We affirmed our 'B-/B' long- and short-term counterparty credit ratings on FirstBank.

At the same time, we have raised our long-term national scale rating on FirstBank to 'ngBB+' from 'ngBB', while we have affirmed our short-term national scale rating at 'ngB'.

Furthermore, we took the same rating actions on FirstBank's nonoperating holding company (NOHC), FBN Holdings PLC (FBNH).

## Rationale

The rating actions reflect our view that FirstBank's regulatory capital has improved and the risk of breaching regulatory requirements has thus diminished. In addition, the bank's funding and liquidity remain a credit strength. Although asset quality remains a weakness, in our view, it is stabilizing thanks to the steadying of the oil price and new management's efforts. We expect FirstBank will continue to display weaker asset quality metrics and lower profitability than other rated top-tier banks in Nigeria in 2017 due to continuing high credit costs. That said, we believe that the bank's new leadership team will address the legacy asset quality issues and institute more prudent risk management measures.

Cost of risk jumped to 10.4% at year-end 2016 from 5.7% at year-end 2015, and nonperforming loans (NPLs) increased to 24.4% for the same period compared with

18.1% the prior year. The performance of the bank's portfolio stems from high concentration and foreign currency loans (51% of total loans in 2016), particularly the oil and gas-related exposures. This performance and the huge impairments have prompted the bank to recruit a new Chief Risk Officer and launch a review of its risk management process to improve loans approvals, risk monitoring, and collection. The bank is also in the process of de-risking its loan portfolio by converting some of its vulnerable foreign currency exposures to local currency. In our opinion, cost of risk will remain high and above the sector average, but decline to 5.3% over the next 12-18 months, while we think NPLs will drop below 20%. At year-end 2016, the bank restructured 5% of its portfolio, with the oil and gas sector accounting for 70% of the total. We expect FirstBank to continue to restructure some loans, particularly in the downstream oil, manufacturing, and general commerce sectors in 2017.

We anticipate that our risk-adjusted capital (RAC) ratio for the bank will decline slightly below 5% in the next 12-18 months. This will result from the bank's risk asset growth moderately outpacing internal capital generation, based on our assumption of a 20% devaluation of the Nigerian naira (NGN) in 2017 and high credit costs. On Dec. 31, 2016, FirstBank's CAR improved to 17.8% from 15.4% on June 30, 2016, following a write back of a capital charge of NGN29 billion (\$95 million) for exceeding the related party single obligor limit and an increase in retained earnings. FirstBank raised U.S. dollar funding in 2013 and 2014, which underpins its long dollar position at year-end 2016. The bank's U.S. dollar-denominated subordinated debt provides a natural hedge to its capital position in the scenario of naira depreciation.

Positively, we view the bank as well-positioned in Nigeria's competitive banking sector, thanks to its large retail footprint, low cost of funding, and stable deposit base. On Dec. 31, 2016, FirstBank recorded a stable funding ratio of 125%, supported by a high proportion (66%) of deposit funding. The bank's foreign currency maturity profile displayed positive gaps at year-end 2016. Net broad liquid assets covered 54% of short-term deposits, comparing well with peers. However, similar to other banks operating in Nigeria, FirstBank's deposit base is somewhat confidence sensitive, due to its contractually short-term nature.

The ratings on the bank reflect the overall creditworthiness of the FirstBank group, whose group credit profile (GCP) we assess at 'b-'. The bank is the core component of the group, which is one of the largest in the Nigerian financial services industry, with a significant retail franchise, providing it with a leading deposit franchise and good naira liquidity.

Despite the bank's high systemic importance, the ratings on FirstBank reflect our assessment of the bank's core group status to the FirstBank group and its GCP of 'b-'. We classify the likelihood of support from the Nigerian government to systemically important banks as uncertain and, as such, we do not factor into the ratings any uplift above the bank's stand-alone credit profile (SACP).

Our ratings on FirstBank's holding company FBNH are at the same level as the ratings on FirstBank, reflecting the absence of debt at the holding company level. Under our

criteria, we generally notch down from the GCP to reflect the structural subordination of the NOHC and its exposure to potential regulatory intervention. Nevertheless, in FBNH's case, we take into account the absence of debt at the holding company level and believe that the risk of the NOHC defaulting is not commensurate with the 'CCC' rating category.

## Outlook

The stable outlook on FirstBank reflects our view that the bank will maintain its CAR above the minimum requirement of 15% over the next 12 months, despite our expectation that risk-weighted asset growth will moderately outpace internal capital generation. It also reflects our view that asset quality will continue to stabilize, although still at weak levels, while the bank will maintain its above average funding and adequate liquidity over the next 12 months.

We could lower the ratings on FirstBank if we saw a sharp deterioration of capitalization due to higher risk weights (caused by a devaluation of the naira) or weaker asset quality due to higher credit losses than anticipated.

A positive rating action on FirstBank would depend on the bank substantially improving its asset quality indicators, while maintaining its capitalization, business position, and funding and liquidity at levels commensurate with a higher rating.

## Ratings Score Snapshot

	To	From
<b>Holding Company Rating</b>	B-/Stable/B	B-/Negative/B
<b>Issuer Credit Rating</b>	B-/Stable/B	B-/Negative/B
<b>SACP</b>	b-	b-
Anchor	b	b
Business Position	Adequate (0)	Adequate (0)
Capital and Earnings	Weak (0)	Weak (0)
Risk Position	Moderate (-1)	Moderate (-1)
Funding and Liquidity	Above Average And Adequate (0)	Above Average And Adequate (0)
<b>Support</b>	0	0
ALAC Support	0	0
GRE Support	0	0
Group Support	0	0
Sovereign Support	0	0
<b>Additional Factors</b>	0	0

## Related Criteria And Research

### Related Criteria

- General Criteria: National And Regional Scale Credit Ratings - September 22,2014
- Criteria - Financial Institutions - Banks: Revised Market Risk Charges For Banks In Our Risk-Adjusted Capital Framework - June 22,2012
- Criteria - Financial Institutions - Banks: Bank Hybrid Capital And Nondeferrable Subordinated Debt Methodology And Assumptions - January 29, 2015
- General Criteria: Group Rating Methodology - November 19,2013
- Criteria - Financial Institutions - Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions - July 17,2013
- General Criteria: Use Of CreditWatch And Outlooks - September 14,2009
- Criteria - Financial Institutions - Banks: Banks: Rating Methodology And Assumptions - November 09,2011
- Criteria - Financial Institutions - Banks: Banking Industry Country Risk Assessment Methodology And Assumptions - November 09,2011
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings - April 07,2017
- Criteria - Financial Institutions - Banks: Bank Capital Methodology And Assumptions - December 06,2010
- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables - June 01,2016
- General Criteria: Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings - October 01,2012

## **Ratings List**

	Rating	
	To	From
First Bank of Nigeria Ltd.		
Counterparty Credit Rating		
Foreign and Local Currency	B-/Stable/B	B-/Negative/B
Nigeria National Scale	ngBB+/-/-/ngB	ngBB/-/-/ngB
Subordinated		
Foreign Currency	CCC	CCC
FBN Finance Company B.V.		
Subordinated		
Foreign Currency	CCC	CCC
FBN Holdings PLC		
Counterparty Credit Rating		
Foreign and Local Currency	B-/Stable/B	B-/Negative/B

	Rating	
	To	From
Nigeria National Scale	ngBB+/--/ngB	ngBB/--/ngB

## Regulatory Disclosures

First Bank of Nigeria Ltd.

FBN Holdings PLC

- Primary Credit Analyst: Kuziva Murigo, Rating Analyst
- Rating Committee Chairperson: John Gibling
- Date initial rating assigned: June 11, 2013
- Date of previous review: April 18, 2017

## Disclaimers

This rating has been determined by a rating committee based solely on the committee's independent evaluation of the credit risks and merits of the issuer or issue being rated in accordance with S&P Global Ratings published criteria and no part of this rating was influenced by any other business activities of S&P Global Ratings.

This credit rating is solicited. The rated entity did participate in the credit rating process. S&P Global Ratings did have access to the accounts, financial records and other relevant internal, non-public documents of the rated entity or a related third party. S&P Global Ratings has used information from sources believed to be reliable but does not guarantee the accuracy, adequacy, or completeness of any information used.

## Glossary

- Adjusted assets: Total assets less nonservicing intangibles.
- Anchor: The starting point for assigning a bank a long-term rating, based on economic and industry risk.
- Asset-liability mismatch: Occurs when financial terms of an institution's assets and liabilities do not correspond.
- Asset quality: A key measure of the quality and performance of the assets of a bank.
- Available stable funding: Core deposits, plus deposits due to banks (net of those that mature within one year), plus other borrowings (net of maturities within one year), plus total equity, minus intangibles.
- Broad liquid assets: cash (net of restricted cash) and reserves at central bank, plus other cash and money market, plus bank loans and reverse repos that mature in less than one year, plus total liquid assets.
- Business position: A measure of the strength of a bank's business operations.
- Capital and earnings: A measure of a bank's ability to absorb losses.
- Core deposits: Total deposits minus noncore deposits (such as deposits due to banks and certificates of deposits).
- Core earnings: Net income before minority interest, minus nonrecurring income, plus nonrecurring expenses, plus/minus tax impact on adjustments, plus

amortization/impairment of goodwill/intangibles, minus preferred dividends.

- Cost of funds: Interest expense as a percentage of average interest-bearing liabilities.
- Counterparty credit rating: A form of issuer credit rating, which is a forward-looking opinion about an obligor's overall creditworthiness.
- Credit losses: Losses arising from credit risk.
- Credit risk: Risk that a borrower will default on its payment obligations.
- Customer loans (gross): Total customer loans before loan loss reserves.
- Customer loans (net) over customer deposits: Gross customer loans net of loan loss reserves, over core deposits.
- Date initial rating assigned: The date S&P Global Ratings assigned the long-term foreign currency issuer credit rating on the entity.
- Date of previous review: The date S&P Global Ratings last reviewed the credit rating on the entity.
- Earning capacity: The capacity of a bank to generate sufficient earnings against losses and the primary way that a bank builds or maintains its capitalization.
- Funding and liquidity: A combined assessment of the strength and stability of a bank's funding mix and its ability to manage its liquidity needs in adverse market and economic conditions over an extended period.
- Funding base: Total deposits, plus acceptances, repurchase agreements, and other borrowings (including commercial papers, short- and long-term debt, subordinated debt, and minimal equity content hybrids).
- Government-related entity (GRE) support: An assessment of the likelihood that the government would provide extraordinary support to a bank that is a government-related entity.
- Gross nonperforming assets over customer loans plus other real estate owned over customer loans: Nonaccrual loans, plus restructured loans, plus repossessed assets plus loans 90-days past due; over gross customer loans plus repossessed assets.
- Group support: An assessment of the likelihood that a parent or other group member would provide extraordinary support to a bank within that group.
- Loan loss reserves over gross nonperforming assets: General plus specific reserves, over adjusted nonperforming assets (nonaccrual loans plus restructured loans plus repossessed assets plus 90-day past due loans).
- National scale rating: An opinion of an obligor's creditworthiness or overall capacity to meet specific financial obligations, relative to other issuers and issues in a given country or region.
- New loan loss provisions over average customer loans: Credit loss provisions (including specific loan provisions and general and other provisions) minus recoveries, over average gross customer loans of current period and last fiscal year.
- Noninterest expenses: Salaries and general administrative expenses (including depreciations and amortizations).
- Normalized credit losses: An assessment of the long-term annualized credit-related losses expected through the credit cycle.
- Operating revenues: Net interest income, plus operating non-interest income (that mainly includes fees and commissions and trading gains)
- Return on equity: Net income before extraordinary results minus preferred dividends over average common (average between current period and last fiscal period).

- Risk position: Our view of the specific risk characteristics of a particular bank.
- Risk-adjusted capital (RAC) ratio before diversification: This is calculated according to S&P Global Ratings' methodology as total adjusted capital over risk-adjusted assets.
- Short-term wholesale funding: Debt securities that mature in less than one year (of commercial papers, debt and senior and subordinated bonds), plus bank deposits that mature in less than one year.
- Sovereign support: An assessment of the likelihood that the government would provide extraordinary support to a bank.
- Stable funding needs: Restricted cash and reserves at the central bank, plus interbank deposits, plus loans to banks (net of maturities within one year), plus reverse repurchase agreements, plus gross customer loans net of loan-loss reserves, plus securities, minus total liquid securities, plus equity participations in nonfinancial entities, plus fixed assets, plus other assets (considering foreclosed assets, tax loss carryforwards, and deferred assets).
- Stable funding ratio: Available stable funding over stable funding needs.
- Stand-alone credit profile (SACP): An interim step in assessing a bank's overall creditworthiness. It includes government support, but not extraordinary government support.
- Total adjusted capital: Adjusted common equity plus admissible preferred instruments and hybrids.
- Total wholesale funding: Noncore deposits, plus acceptances, repurchase agreements, other borrowings (including commercial papers, debt and senior and subordinated bonds, minimal equity content hybrids), and total equity, minus minority interest and common shareholders' equity.

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