FITCH REVISES OUTLOOK ON FBNH TO POSITIVE; AFFIRMS AT 'B-'

Fitch Ratings-London-27 November 2018: Fitch Ratings has revised the Outlook on the Long-Term Issuer Default Ratings (IDR) of FBN Holdings Plc (FBNH) and its primary operating company, First Bank of Nigeria (FBN) to Positive from Negative and affirmed the IDRs at 'B-'. Fitch has also upgraded the National Long- and Short-Term Ratings of FBNH and FBN to 'BBB(nga)' from 'BB+(nga)' and 'F2(nga)' from 'B(nga)', respectively. A full list of rating actions is at the end of this rating action commentary.

The revision of the Outlooks reflects improving asset quality trends and our expectation that the bank's largest impaired loans will be resolved within the Outlook horizon. It also reflects stronger loan loss allowance coverage of impaired loans, under IFRS 9, with this positive trajectory expected to continue. These factors have also driven the upgrade of FBNH's and FBN's National Ratings, given the improvement in their credit profiles relative to other Nigerian issuers.

KEY RATING DRIVERS

IDRS AND VRs

FBNH's and FBN's IDRs are driven by their standalone credit profiles, as defined by their Viability Ratings (VR). Like all Nigerian banks, the VRs are influenced by the operating environment in Nigeria. The fragile economic recovery restrains banks' growth prospects and asset quality. The VRs also reflect FBN's position as one of the country's largest banks and its resilient franchise, which provides robust revenue generation capacity, a solid funding base and sound liquidity.

The VRs also reflect a high, albeit improving impaired loan ratio and improving loan loss allowance coverage, which leaves capital buffers less vulnerable to unexpected shocks.

The operating environment in Nigerian remains tough, with the country having recently emerged from a recession. Although access to foreign currency has eased, many borrowers retain limited capacity to service obligations and there are few opportunities for banks to grow their loan portfolios.

Asset quality remains a relative weakness compared with other large Nigerian banks, illustrated by a far higher impaired loans (Stage 3 loans under IFRS 9)/gross loans ratio of 19.8% at end-9M18 and lower reserve coverage of impaired loans (69%) than peers. However, both metrics are on a positive trend, which we expect to continue in 2019. Loan impairment charges continue to weigh on profitability.

FBNH's Fitch core capital ratio of 18.6% at end-1H18 has been supported by solid pre-impairment earnings and no dividend distributions. While higher reserve coverage takes pressure off capital, FBN's regulatory total capital adequacy ratio would still fall below the minimum regulatory capital requirements if FBN was to fully provide for its impaired loans. This is not our base case, and the bank's internal capital generation could easily make up the shortfall if needed.

Pre-impairment earnings have been resilient, thanks to the group's strong domestic franchise. FBN is the oldest and second-largest bank in Nigeria, with a market share of 14% of domestic credit at end-2017. The franchise has stood up well in the face of asset quality problems. Fitch believes that profitability will strengthen with improving asset quality.

Franchise strength is further illustrated by the group's solid funding base of low cost retail deposits, driving one of the lowest cost of funding in the sector. Cheap, stable funding is complemented by strong liquidity. FBN's regulatory liquidity ratio is well above the minimum requirement of 30% at end-9M18, at 43%. Liquidity is provided by a large book of domestic government securities.

FBNH's and FBN's National Ratings reflect their creditworthiness relative to the country's best credit and relative to peers operating in Nigeria.

SUPPORT RATING AND SUPPORT RATING FLOOR
FBN's Support Rating (SR) and Support Rating Floor (SRF) reflect uncertainty over the ability of the authorities to support banks, particularly in foreign currency. In addition, there are no clear messages from the authorities regarding their willingness to support the banking system. The SRF of all Nigerian banks is 'No Floor' and all Support Ratings are '5', which reflects our view is that senior creditors cannot rely on receiving full and timely extraordinary support from the authorities should a bank become non-viable.

FBNH's SR and SRF reflect our view that any support that could come from the authorities to domestic banks is unlikely to extend to the holding company, which does not have material creditors.

SUBORDINATED DEBT
Subordinated debt issued by FBN's Netherlands -incorporated special purpose vehicle FBN Finance B.V. is rated one notch below FBN's VR to reflect loss severity for subordinated creditors. Recoveries on the notes in the event of default are considered to be below average and therefore the Recovery Rating on the notes is 'RR5'.

RATING SENSITIVITIES
IDRS, VRs, NATIONAL RATINGS AND SENIOR DEBT
FBNH's and FBN's IDRs are both sensitive to any change in their VRs. The Outlooks on the IDRs are Positive, reflecting Fitch's base case that asset quality will see a material improvement. This ultimately considers the resolution of the bank's largest NPL, which is around 8% of gross loans and is expected to be resolved during 2019. Should NPLs decline rapidly and loan loss allowance coverage continue to improve, then the VRs and IDRs could be upgraded.

A downgrade would most likely be as a result from a renewed deterioration in asset quality.

FBNH's and FBN's National Ratings are sensitive to a change in their creditworthiness relative to other Nigerian issuers.

SUPPORT RATING AND SUPPORT RATING FLOOR
FBN's SR could be upgraded and the SRF revised upwards if Fitch sees an improvement in the authorities' ability to support in foreign currency, particularly as a systemically important bank. An improvement in the ability to support could be indicated by further accumulation of external reserves and a sustainable exchange rate. An upward revision of the SRF could lead to an upgrade of FBN's Long-Term IDR. As a holding company, we view an upgrade of FBNH's SR and upward revision of the SRF as unlikely.

SUBORDINATED DEBT
The Long-Term Rating on subordinated debt issued by FBN Finance B.V. is sensitive to any change in FBN's Long-Term IDR.

The rating actions are as follows:

FBN Holdings Plc and First Bank of Nigeria Limited
Long-Term IDRs affirmed at 'B-'; Outlooks revised to Positive from Negative
Short-Term IDRs affirmed at 'B'

Viability Ratings affirmed at 'b-'
Support Rating Floors affirmed at 'No Floor'
Support Ratings affirmed at '5'
National Long-Term Ratings upgraded to 'BBB(nga)' from 'BB+(nga)'
National Short-Term Ratings upgraded to 'F2(nga)' from 'B(nga)'

FBN Finance B.V.
Subordinated debt long-term rating affirmed at 'CCC+'/'RR5'

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Additional information is available on www.fitchratings.com

Applicable Criteria
Bank Rating Criteria (pub. 12 Oct 2018)
https://www.fitchratings.com/site/re/10044408
National Scale Ratings Criteria (pub. 18 Jul 2018)
https://www.fitchratings.com/site/re/10038626