

FSDH Merchant Bank Limited

A financial institution of good financial condition and strong capacity to meet its obligations relative to all other issuers in the same country.

Ratings Assigned:

National Rating: **A**

Foreign Currency (FCY): **B-**

ESG Score:

2

Outlook: Stable

Issue Date: 21 July 2023

Expiry Date: 30 June 2024

Previous Rating:

National Scale: A

FCY Scale: B-

Industry: Banking

Analysts:

Ihuoma Udensi

ihuomaudensi@agusto.com

Ayokunle Olubunmi, CFA

ayokunleolubunmi@agusto.com

Agusto & Co. Limited

UBA House (5th Floor)

57, Marina

Lagos

Nigeria

www.agusto.com

RATING RATIONALE

Agusto & Co. affirms FSDH Merchant Bank Limited's ('FSDH MB' or 'the Bank') 'A' national rating and 'B-' foreign currency rating. The ratings reflect the Bank's good profitability relative to its peers, adequate capitalisation, good liquidity profile and experienced management team. However, constraining these positives are the concentration in the loan book and the fragile state of the Nigerian economy. FSDH MB's FCY rating is reflective of the risk rating of the Federal Republic of Nigeria with a sovereign rating of 'B-' assigned by Agusto & Co. We have also affirmed the '2' ESG score denoting that environmental, social and governance issues have minimal contributions to the Bank's credit risk.

In the year under review, FSDH MB maintained an expansionary stance in risk asset creation as reflected in the 50% year-on-year growth in the loan book to ₦118.5 billion as at FYE 2022. Notwithstanding, obligor concentration remains as the top 10 exposures accounted for 52.4% (FYE 2021: 57.2%) of gross loans as at the same date. The largest exposure which is foreign currency denominated represented 43% (FYE 2021: 40%) of shareholders' funds, higher than the 40% internal guidance, albeit lower than the 50% regulatory maximum. The Bank's impaired (stage 3) loans declined by a marked 46.3% to ₦1.9 billion on the back of write offs. As a result, the impaired loan ratio plummeted to 1.7% (FYE 2021: 4.7%), lower than the 5% threshold and the cumulative loan loss provisions improved to 212.9% (FYE 2021: 121%). We consider FSDH MB's asset quality to be acceptable, although we believe that it will remain pressured by the fragile macro-economic environment.

FSDH MB leverages innovation and a role as a collections bank for some corporate and public sector entities to drive liability generation. As at 31 December 2022, the total deposit liabilities stood at ₦98.2 billion, up by 36.9% on the back of an intensified deposit mobilisation drive. However, low-cost deposits represented a lower 33.2% of total deposit liabilities, reflecting the wholesale focus of the Bank and rising yields. Consequently, the weighted average cost of funds (WACF) pushed up to 8.7% (FY 2020: 5.9%) in FY 2022. Nevertheless, the WACF was one of the lowest in the merchant banking segment in the year under review due to low-cost funding initiatives by the

The copyright of this document is reserved by Agusto & Co. Limited. No matter contained herein may be reproduced, duplicated or copied by any means whatsoever without the prior written consent of Agusto & Co. Limited. Action will be taken against companies or individuals who ignore this warning. The information contained in this document has been obtained from published financial statements and other sources which we consider to be reliable but do not guarantee as such. The opinions expressed in this document do not represent investment or other advice and should therefore not be construed as such. The circulation of this document is restricted to whom it has been addressed. Any unauthorized disclosure or use of the information contained herein is prohibited.

Bank. The Bank liquidity ratio also improved to 39.3% (FYE 2021: 26%) and remained comfortably above the 20% regulatory minimum for merchant banks. The Bank's ability to refinance also remains strong upheld by its good brand name as reflected in the successful issuances of commercial papers and debt instruments. FSDH MB is well capitalised for current level of business risks with a capital adequacy ratio (CAR) of 20.2%, higher than the regulatory minimum of 10% for merchant banks.

Profitability improved markedly in the 2022 financial year on account of an expanded loan book, upward loan repricing and significant increase in trading gains. The net earnings rose by 70.5% to ₦10.3 billion, moderating the cost-to-income ratio to 60.9% from the 83.4% recorded in the prior year; despite the 24.4% increase in operating expenses. Overall, the profit before tax surged 4 times to ₦4 billion, and translated to improved profitability metrics; pre-tax return on average assets and contingents (ROA) of 1.6% (FY 2021: 0.5%) and pre-tax return on average equity (ROE) of 14% (FY 2021: 3.6%), to make FSDH MB the second most profitable merchant bank in Nigeria in FY 2022. We view positively the improved profitability and anticipate that this level of performance should be sustained based on the projected loan book growth and plans to continue to leverage the expertise in treasury and corporate banking. Subsequent to the year end, in the first five months ended 30 May 2023, the annualised ROA and ROE strengthened further to 2.4% and 23.9% respectively.

Based on the aforementioned, we attach a **stable** outlook to the rating of FSDH Merchant Bank Limited.

Strengths	<ul style="list-style-type: none"> • Good profitability • Expertise in treasury activities • Membership of a financial holding company with presence in different segments of the financial sector • Experienced management team
Weaknesses	<ul style="list-style-type: none"> • Obligor concentration in the loan book • High cost of risk relative to peers
Challenges	<ul style="list-style-type: none"> • The impact of the weak macroeconomic climate on businesses • Maintaining good asset quality as the Bank expands its loan book • Retaining quality employees in the face of an emigration wave

Table 1: Background Information

	31 December 2021	31 December 2022
Total Assets & Contingents	₦213.7 billion	₦286.1 billion
Net Earnings	₦6 billion	₦10.3 billion
Pre-tax Return on Average Assets & Contingents (ROA)	0.5%	1.6%
Pre-tax Return on Average Equity (ROE)	3.6%	14%

PROFILE

FSDH Merchant Bank Limited ('FSDH MB' or the 'Bank') was incorporated in June 1992 as First Securities Discount House Limited and commenced operations in March 1993. Following the review of the banking regulatory framework and the re-introduction of the merchant banking business model, it converted to a merchant bank in November 2012. Thereafter, the Bank's name was changed to FSDH Merchant Bank Limited and merchant banking operations commenced in January 2013. In 2019, a restructuring exercise was conducted and FSDH Holding Company Limited (the HoldCo), a non-operating legal entity domiciled in Nigeria and regulated by the Central Bank of Nigeria (CBN) was incorporated and became the parent company of the Bank. Consequently, FSDH Merchant Bank Limited transferred its ownership stake in its hitherto subsidiaries (FSDH Asset Management Limited, Pensions Alliance Limited and FSDH Capital Limited) to the HoldCo.

FSDH Merchant Bank Limited is one of the six merchant banks operating in Nigeria. The services offered by the Bank include transactional and structured finance, money market activities including trading and holding of marketable securities such as treasury bills, government bonds, commercial bills and other eligible instruments. FSDH MB's activities are organised into three business divisions; Global Markets/Prestige Banking Corporate Banking and Business Banking.

Ownership and Support

FSDH Merchant Bank Limited is a wholly-owned subsidiary of FSDH Holding Company Limited, a non-operating legal entity regulated by the CBN. The HoldCo is a closely held company with five significant shareholders that together controlled 92.84% of the shareholding as at 31 December 2022.

Table 2: Significant Shareholders of FSDH Holding Company Limited

Shareholder	Equity Stake
KMC Investments Limited	32.04%
Atlantic Coast Regional Fund	23.25%
Kuramo Africa Opportunity Nigerian Vehicle Limited	16.35%
United Capital Asset Management Limited	10.80%
FSDH Staff Co-operative Society	10.40%
Total	92.84%

Board of Directors

FSDH MB is governed by a nine-member Board of Director comprising three Executive Directors and six Non-Executive Directors (including two Independent Non-Executive Director). The Board's oversight functions are executed through four standing committees: the Board Audit Committee, the Board Risk Committee, the Board Governance and Nominations Committee, and the Board Finance and Strategy Committee. During the year under review, Mr. Tosa Ogbomo, a Non-Executive Director, resigned while Ms. Stella-Marie Omogbai was appointed as an Executive Director subsequent to the year end.

Ms. Stella-Marie Omogbai currently heads the corporate banking division at FSDH Merchant Bank Limited. She has circa three decades of professional experience in the banking industry garnered from Bank PHB Plc (now Keystone Bank Limited), Access Bank Plc, United Bank for Africa Plc, Ecobank Limited, amongst others. Ms. Omogbai holds a Bachelor of Laws degree from the University of Benin, Edo State and is also a graduate of the Nigerian Law School. She also holds a Masters in Business Administration (MBA) from the University of Wales, United Kingdom and has participated in several senior management courses both locally and internationally.

CURRENT DIRECTORS

DESIGNATION

Mr Olufemi Agbaje

Chairman

Mrs Bukola Smith

Managing Director

Mr Taiwo Otiti

Executive Director

Ms. Stella-Marie Omogbai*

Executive Director

Prof. Isabella Okagbue

Non-Executive Director

Mr Patrice Backer

Non-Executive Director

Mr Kelechi Okoro

Non-Executive Director

Mr Godwin Ize-Iyamu

Independent Non-Executive Director

Mr. Musa Ali Baba

Independent Non-Executive Director

**Appointed January 2023*

Management & Staff

Mrs Bukola Smith is the Managing Director of FSDH Merchant Bank Limited. She has three decades of experience in the banking industry traversing various roles including treasury, capital markets, investment banking, private banking, structured finance, internal audit, and business development. She has expertise in strategy, execution, innovation and commercial leadership. Prior to her appointment, she served as the Executive Director, Business Development at First City Monument Bank (FCMB) Limited where she was responsible for over 200 branches across the country. Mrs Smith also worked at FSB International Bank (now part of Fidelity Bank Plc) where she commenced her career in 1992. She holds a B.Sc. in Economics from the University of Lagos and a Master's in Business Administration (MBA) from Alliance Manchester Business School,

Manchester, UK. Mrs Smith is an Honorary Fellow of the Institute of Chartered Accountants of Nigeria (ICAN) and an Associate Member of the Certified Institute of Pensions (Nigeria). She currently sits on the Board of Women in Successful Careers (WISCAR) and the Toyin Oni Foundation (NGO for cancer awareness).

Other members of FSDH Merchant Bank Limited's senior management team include:

Mr Taiwo Otit	Executive Director, Operations, Information Technology and Compliance
Ms. Stella-Marie Omogbai	Executive Director, Corporate Banking and Branches
Mr Richard Osuagwu	Chief Risk Officer
Mr Hakeem Muhammed	Head, Global Markets and Prestige Banking
Mr Babatunde Obidare	Group Head, Operations
Mr Kunle Osunkunle	Head, Corporates
Mrs Bukola Lanipekun Lawal	Head, Human Resources
Mr Taiwo Sanusi	Chief Compliance Officer
Mr Adediran Oni	Head, Energy
Mr Dennis Ezaga	Head, Business Banking
Mr Oluwaseun Omole	Chief Financial Officer
Ms Bolanle Meshida	Head, Legal and Company Secretary

During the year under review, the Bank employed an average of 146 persons, higher than the 120 persons in FY 2021. Given the expansion of the staff strength and higher remuneration to support staff retention, personnel costs rose by 19.2% and the average cost per staff increased by 6.2% to ₦18.1 million. Underpinned by the significant improvement in earnings, net earnings per staff spiked by 51.8% to ₦70.6 million and was sufficient to cover average staff cost 3.9 times (2021: 2.7 times), better than the merchant banking segment's 3.4 times. In our opinion, FSDH MB's staff productivity is good and we believe the Bank is led by an experienced management team.

ANALYSTS' COMMENTS

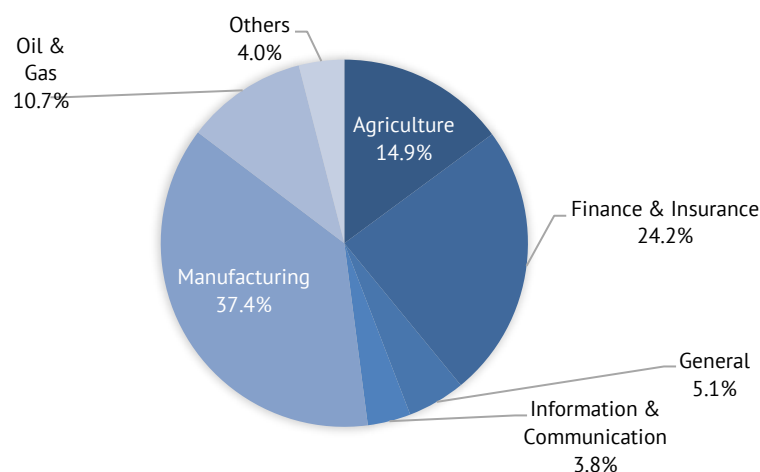
ASSET QUALITY

Over the years, FSDH MB's lending strategy has been focused on providing financial solutions to top-tier corporates operating in selected economic sectors. However, the quest to improve yields has resulted in a cautious foray to mid-sized obligors that are typically less sensitive to loan pricing. Following a review of the business strategy and fortification of the risk management appropriately, the Bank grew the loan book by 50% to ₦118.5 billion as at 31 December 2022.

Notwithstanding, the loan portfolio remained concentrated as the top 10 obligors accounted for 52.4% (FYE 2021: 57.2%) of gross loans as at FYE 2022. While this level of concentration is pervasive in the merchant bank segment, we believe it increases the vulnerability of FSDH MB's asset quality to a decline in the performance of these obligors. As at FYE 2022, the largest exposure, which is denominated in foreign currency, is to an upstream oil and gas firm and accounted for a notable 43% (FYE 2021: 40%) of shareholders' funds, higher than the 40% internal guidance although lower than the 50% regulatory limit. We are wary that the naira devaluation associated with the unification of exchange rates could further bloat the exposure. However, the Bank has disclosed repayment plans which is expected to keep the naira value below the regulatory threshold.

As at FYE 2022, the manufacturing, finance & insurance and agriculture sectors dominated the loan book and jointly constituted 76.5% (FYE 2021: 56.6%). Although the manufacturing sector is a conglomeration of different industries, the naira devaluation has raised the cost of input (which are predominantly imported) while the declining consumer purchasing power has moderated demand. The finance & insurance sector is a key focus area of the Bank leveraging its asset backed lending product to financial institutions while FSDH MB took advantage of opportunities during the year to fund exporters in the agro-allied space to support FCY deposits.

Figure 1: Breakdown of Loan Book by Sector (FYE 2022)



As at FYE 2022, 98% (FYE 2021: 95.3%) of the Bank's loan portfolio was classified under the stage 1 category while no loan was in the stage 2 category. However, stage 3 loans declined by 46.3% to ₦1.9 billion driven by the ₦2.2 billion write off of an impaired facility in the technology sector. This translated to an impaired loan ratio of 1.7% (FYE 2021: 4.7%), well below the regulatory guidance of 5% but higher than selected peers; FBNQuest Merchant Bank Limited (FBNQuest MB) and Coronation Merchant Bank Limited (Coronation MB) with 1.4% and nil impaired loan ratio respectively. As at FYE 2022, the cumulative loan loss provisions (including regulatory risk reserves) covered the impaired loans by 212.9% (FYE 2021: 121%), which is good in our view.

We consider FSDH MB's asset quality to be acceptable by industry standards. However, we believe that the fragile macroeconomic environment will continue to exert pressure on the asset quality. The Bank projects a 11.2% loan growth in FY 2023, largely driven by agro-allied businesses with export potentials and healthcare businesses. We view the projected loan book growth as achievable.

RISK MANAGEMENT

FSDH MB utilises a credit risk rating model which considers both quantitative and qualitative factors in the measurement of the risk profile of obligors. As at FYE 2022, 90% (FYE 2021: 95.2%) of the Bank's obligors were categorised as investment grade while the balance of 10% (FYE 2021: 4.8%) were speculative grade obligors. As at the same date, approximately 13% of the loan book was secured with a collateral coverage of 98.7%. We believe that the credit risk of the Bank like most banks is vulnerable to the prevailing macroeconomic weaknesses.

A sensitivity analysis conducted as at FYE 2022 revealed that a 100-basis point increase in the interest rates would have reduced the Bank's profit before tax by ₦74.8 million, 0.03% of the shareholders' funds. Similarly, devaluation of the naira by 2000-basis points naira would have led to a potential loss of ₦473.6 million (0.2% of shareholders' funds), which we consider to be immaterial. In FY 2022, the Bank incurred penalties amounting to ₦17.2 million, 8.2 times higher than the prior year, for misreporting currency transaction report (CTR) returns during the CBN's anti-money laundering (AML) risk-based audit.

We consider FSDH MB's risk management framework to be adequate for the current level of business risks undertaken.

EARNINGS

Despite the prevailing macroeconomic and regulatory headwinds, FSDH MB's performance improved significantly in the year under review on the back of a better understanding of the heterodox monetary policies and recalibration of the business strategy. The Bank emphasised liquidity management and leveraged arbitrage opportunities in the market to grow trading income. As a result, the net earnings improved by 70.5% to ₦10.3 billion with fund-based income contributing 44.6% (FY 2021: 55.3%), while the remaining 55.4% (FY 2021: 44.7%) emanated from non-interest income.

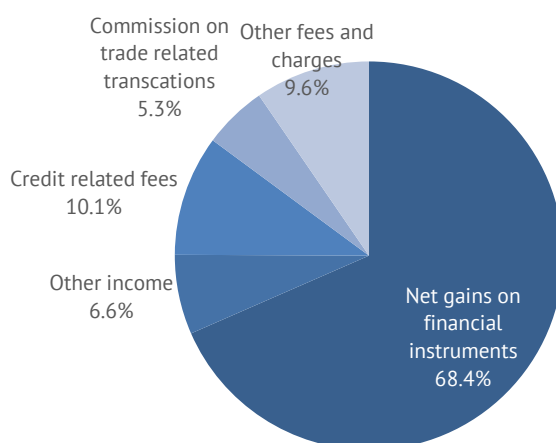
During the year under review, interest income surged by 69%, buoyed by the expanded loan book, loan repricing and a larger pool of investment securities. However, interest expenses also rose in tandem by 68.7%

to ₦90.5 billion due to expanded borrowings in a rising yield environment. Notwithstanding, the net interest spread (NIS) remained stable at 31.8% and was better than Coronation MB's -13.2%, FBNQuest MB's 17.5% and the merchant banking segment average of 14.3%. We believe that the NIS will remain pressured by the rising interest rate environment given that deposit liabilities will be quickly repriced than loans, the wholesale focus of the Bank and the rate sensitivity of its institutional depositors. Subsequent to the year end, based on the unaudited financial statements ended 31 May 2023, the NIS declined to 25.8%, reflecting our expectations.

In FY 2022, FSDH MB charged off ₦1.3 billion as impairment charges, 9 times higher than the previous year buoyed by the significant loan book growth and write-offs. Thus, the loan loss expense to interest income ratio rose to 7.1% (FY 2021: 1.3%) and translated to a higher cost of risk of 1.3% (FY 2021: 0.2%). The write off was on a lingering exposure which the Bank decided to take off its books. Barring any unforeseen contingencies, we anticipate a decline in the impairment charges in the near term as the Bank maintains a cautious approach to lending.

Since transition to a merchant bank in 2013, FSDH MB has consistently relied on non-interest income as a significant contributor to its earnings, leveraging the treasury competencies developed from the precursor institution. During the year under review, opportunities in the treasury bills market, customised derivative solutions, credit related fees from the expanded loan book and the sustained digital push supported non-interest income. As a result, the non-interest income surged 2.1 times to ₦5.7 billion and represented 2% (FY 2021: 1.3%) of total assets and contingents, better than Coronation MB's 0.7%, though lower than FBNQuest MB's 2.6%. We anticipate further increase in the non-interest income supported by the normalisation of monetary policies and liberalisation of the foreign exchange market. Credit related fees from the loan book expansion will also be positive for non-interest income in the near term.

Figure 1: Breakdown of Non-Interest Income in FY 2022



Driven by the intense inflationary pressures, business growth and upward review of staff salaries, FSDH MB's operating expenses trended upwards by 24.4% to ₦6.3 billion. However, the significant improvement in earnings moderated the cost-to-income ratio (CIR) materially to 60.9% from 83.4% in the previous year. The

CIR stood better than selected peers and the estimated merchant banking industry average of 70%. We believe that the raging inflationary wave, exacerbated by the removal of fuel subsidy and naira devaluation, could exert pressure on the CIR in the near term though tempered by anticipated further improvements in net earnings.

Despite economic challenges, FSDH MB's profitability compared better than most of its peers in the merchant banking segment. Profitability improved markedly with pre-tax return on average assets and contingents (ROA) of 1.6% (FY 2021: 0.5%) and a pre-tax return on average equity (ROE) of 14% (FY 2021: 3.6%). Subsequent to the year end, based on the unaudited financial statements for the first five months ended 31 May 2023, the profitability metrics strengthened further with annualised ROA and ROE of 2.4% and 23.9% respectively. We expect FSDH MB's performance should continue to compare well with its peers in the merchant banking segment given its good revenue generation, strategic funding initiatives and conservative risk management stance.

CAPITAL ADEQUACY

As at 31 December 2022, FSDH MB's shareholders' funds stood at ₦25 billion, down by 6.7% from the prior year due to a ₦4.4 billion fair value loss incurred on financial assets classified as fair value through other comprehensive income. Notwithstanding, the shareholders' funds remained well above the ₦15 billion regulatory minimum for merchant banks. The tier 2 capital dipped by 54.3% year on year to ₦2.6 billion as at FYE 2022, subdued by the fair value losses recorded on financial assets.

FSDH MB's capital adequacy ratio (CAR) was stable at 20.2% as at FYE 2022, and remained comfortably above the 10% regulatory minimum for merchant banks. Furthermore, the CAR compared favourably with selected peers; Coronation MB at 10.3% and FBNQuest MB at 16.3%. We consider FSDH MB's capital to be satisfactory for the current level of business risks taken.

LIQUIDITY AND LIABILITY GENERATION

FSDH Merchant Limited is primarily funded by liabilities generated from corporates, institutional investors, public sector and financial institutions. Growing affinity with the financial technology companies (FinTechs) and the public sector (through tax collection) in addition to collection solutions provided for corporates have supported a wider and low-cost funding base, relative to peers. As at 31 December 2022, the total deposit liabilities stood at ₦98.2 billion, 36.9% higher than the previous year. The short nature of deposits from the FinTechs, low appetite for trade finance transactions (which require customers to build up cash for bid at the foreign exchange market) and rising yield environment resulted in a 30.7% growth in the relatively expensive tenored deposits. Consequently, the deposit mix deteriorated as tenored funds represented 66.8% (FYE 2021: 48.5%) of total deposits, albeit lower than Coronation MB's 91% and FBNQuest MB's 98.4%. Given the liberalisation of the foreign exchange market and the associated unification of the exchange rate, we anticipate an increased appetite for trade finance transactions which should support low-cost deposits in the near term.

During the year under review, FSDH MB leveraged the illiquidity in the foreign exchange market to introduce innovative solutions to clients while also supporting businesses with foreign currency earnings. As a result, foreign currency-denominated (FCY) deposits grew by 66.1% to ₦31.8 billion and funded 64% (FYE 2021: 60.7%) of FCY loans as at FYE 2022. We anticipate a further increase in the foreign currency denominated deposits in the near term based on the various growth initiatives of the Bank.

FSDH MB's activities are also funded by borrowings from multinational financial institutions (MFIs), debt capital market and the interbank market. During the year under review, new borrowings were sourced from MFIs for on-lending to the real sector while additional commercial papers were issued to support trade transactions. As a result, the outstanding borrowings rose by 49.6% year on year to ₦58.9 billion and accounted for 20.6% (FYE 2021: 18.4%) of total assets and contingents as at FYE 2022.

Given the deterioration in the funding mix amidst rising rates and expanded borrowings, FSDH MB's weighted average cost of funds (WACF) increased to 8.7% (FY 2021: 5.9%), but compared favourably with Coronation MB's 10.5% and the estimated merchant banking segment average of 9%, though higher than FBNQuest MB's 7.7%. We anticipate that the WACF may increase further in tandem with the rising yield environment, though moderated by the various initiatives of the Bank to ramp up low-cost deposits.

FSDH MB's liquid assets, which largely comprised government securities stood at ₦25.4 billion, representing a significant 94% year-on-year growth. As a result, the liquidity ratio increased to 39.3% (FYE 2021: 26%) and remained above the 20% regulatory minimum for merchant banks operating in Nigeria. A breakdown of the maturity profile of FSDH MB's loans vis-à-vis deposits and borrowings showed gaps in all the categories except the 'within 30 days' and '180-360 days' maturity buckets, exposing the Bank to potential repricing risks. However, the large pool of treasury securities and access to the money market, serve as mitigants.

We consider FSDH MB's liquidity profile to be good and its ability to refinance remains strong, upheld by its good brand name.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE

Based on our assessment, the contribution of environmental and social issues to the credit rating assigned to FSDH MB is low. In our view, the Bank has a good corporate governance structure, with good succession planning. This was reflected in the successful change in the executive management team, twice since the transition to a merchant bank. However, we believe further gender diversity is required at the Board, where females constituted 22%, below the 30% benchmark of the Central Bank of Nigeria. Furthermore, females in the senior management level represented 21%, lower than the 40% threshold.

Although exposure to the oil and gas sector has potential for environmental risk, we note the environmental impact study and other measures introduced to ensure that the activities of the oil and gas obligors, particularly those in the upstream segment have a minimal adverse impact on the environment. The Bank also embeds environmental, social and governance considerations in credit approval processes and in the day-to-day

operational activities. As at 31 December 2022, 20% of the loan book were disbursed to socially critical sectors (agriculture, human health and social work activities). Overall, we consider the contribution of environmental, social and governance issues to FSDH MB's credit rating to be minimal.

MARKET SHARE

FSDH Merchant Bank Limited is one of the discount houses that transformed to merchant banks. FSDH is the 4th largest merchant banks by total assets as at FYE 2022. The Bank recorded marked improvement in profitability in the year under review. On this basis, the Bank is the second most profitable merchant bank in the financial year ended 31 December 2022 as emphasis was on performance and to a lesser extent size. The share of local currency deposits increased on the back of collections and other funding initiatives. We expect the positive performance trajectory to be sustained as the Bank continues to leverage technology to attract relatively lower-priced deposits to maximise earnings while growing risk assets to select sectors of the economy.

Figure 2: Market Share of the Merchant Banking Segment as at FYE 2022

	FSDH MB 2021	FSDH MB 2022	Coronation MB 2022	Greenwich MB 2022	FBNQuest MB 2022	Nova MB 2022	Rand MB 2022
Total Assets & Contingents	14.3%	14.4%	32.4%	5.2%	15.3%	16%	16.7%
Net Loan	21%	18.2%	28.8%	5.1%	16.5%	15.1%	16.3%
LCY Deposits	13%	15.6%	39.1%	6.7%	17.5%	21.9%	4.9%
Net Earnings	12%	19.4%	0.2%	8.1%	18.2%	13.6%	40.5%
Pre-tax Profit	5%	25.3%	-51.6%	8.3%	18.8%	21.6%	77.7%

OUTLOOK

FSDH MB has disclosed some key strategic initiatives to sustain the positive performance recorded during the last financial year to be intensifying liquidity management strategies in order to effectively seize business opportunities and strengthening relationships with aggregators to accumulate lower-cost funding. Furthermore, the Bank has created an e-channels team to man virtual channels to drive operational efficiency and bolster overall performance. FSDH MB projects an 11.2% growth in the loan book, with some opportunities for the risk asset creation identified in the healthcare and agro-allied space.

Overall, we anticipate that FSDH MB's performance trajectory will be sustained in the near term based on the aforementioned growth initiatives, in addition to the strong treasury function which should continue to support ancillary earnings. We expect that liquidity and capitalisation should remain adequate while ability to refinance remains good, upheld by its conservative antecedence and brand name. However, in our view, the macroeconomic headwinds could further exert pressure on the asset quality, particularly given the foray to

relatively riskier mid-sized obligors while rising inflation would adversely impact cost of operations. Nonetheless, we expect the Bank's robust risk management framework will continue to uphold asset quality.

Based on the aforementioned, we have attached a ***stable*** outlook to the rating of FSDH Merchant Bank Limited.

FINANCIAL SUMMARY

FSDH MERCHANT BANK LIMITED

STATEMENT OF FINANCIAL POSITION AS AT	31-Dec-2020 N'millions		31-Dec-2021 N'millions		31-Dec-2022 N'millions	
ASSETS						
1 Cash & equivalents	2,001	1.1%	115	0.1%	3,323	1.2%
2 Government securities	16,019	9.1%	5,207	2.4%	17,839	6.2%
3 Money market placements	4,003	2.3%	7,783	3.6%	4,304	1.5%
4 Quoted investments						
5 Placements with discount houses						
6 LIQUID ASSETS	22,023	12.6%	13,105	6.1%	25,466	8.9%
7 BALANCES WITH NIGERIAN BANKS	397	0.2%	585	0.3%	644	0.2%
8 BALANCES WITH BANKS OUTSIDE NIGERIA	20,485	11.7%	12,653	5.9%	12,665	4.4%
9 Direct loans and advances - Gross	40,314	23.0%	79,045	37.0%	118,564	41.4%
10 Less: Cumulative loan loss provision	(2,242)	-1.3%	(2,418)	-1.1%	(1,353)	-0.5%
11 Direct loans & advances - net	38,072	21.7%	76,627	35.8%	117,211	41.0%
12 Advances under finance leases - net						
13 TOTAL LOANS & LEASES - NET	38,072	21.7%	76,627	35.8%	117,211	41.0%
14 INTEREST RECEIVABLE						
15 OTHER ASSETS	1,168	0.7%	4,009	1.9%	16,955	5.9%
16 DEFERRED LOSSES	2,599	1.5%	2,527	1.2%	2,238	0.8%
17 RESTRICTED FUNDS	27,062	15.4%	30,846	14.4%	26,562	9.3%
18 UNCONSOLIDATED SUBSIDIARIES & ASSOCIATES						
19 OTHER LONG-TERM INVESTMENTS	46,562	26.6%	47,300	22.1%	54,220	18.9%
20 FIXED ASSETS & INTANGIBLES	1,080	0.6%	1,061	0.5%	1,068	0.4%
21 TOTAL ASSETS	159,449	91.0%	188,713	88.3%	257,029	89.8%
22 TOTAL CONTINGENT ASSETS	15,766	9.0%	25,061	11.7%	29,148	10.2%
23 TOTAL ASSETS & CONTINGENTS	175,215	100%	213,774	100%	286,177	100%
CAPITAL & LIABILITIES						
24 TIER 1 CAPITAL (CORE CAPITAL)	28,045	16.0%	28,213	13.2%	29,505	10.3%
25 TIER 2 CAPITAL	2,769	1.6%	5,685	2.7%	2,598	0.9%
26 Medium to long-term borrowings	23,050	13.2%	39,397	18.4%	58,930	20.6%
27 Demand deposits	20,185	11.5%	26,761	12.5%	32,589	11.4%
28 Savings deposits						
29 Time deposits	40,806	23.3%	25,854	12.1%	33,800	11.8%
30 Inter-bank takings	19,621	11.2%	26,148	12.2%	30,188	10.5%
31 TOTAL DEPOSIT LIABILITIES - LCY	80,612	46.0%	78,763	36.8%	96,577	33.7%
32 Customers' foreign currency balances	19,223	11.0%	19,180	9.0%	31,862	11.1%
33 TOTAL DEPOSIT LIABILITIES	99,835	57.0%	97,943	45.8%	128,439	44.9%
34 INTEREST PAYABLE						
35 OTHER LIABILITIES	5,749	3.3%	17,475	8.2%	37,557	13.1%
36 TOTAL CAPITAL & LIABILITIES	159,449	91.0%	188,713	88.3%	257,029	89.8%
37 TOTAL CONTINGENT LIABILITIES	15,766	9.0%	25,061	11.7%	29,148	10.2%
38 TOTAL CAPITAL, LIABILITIES & CONTINGENTS	175,215	100%	213,774	100%	286,177	100%
BREAKDOWN OF CONTINGENTS						
39 Acceptances & direct credit substitutes	23,725	13.5%	18,389	8.6%	11,517	4.0%
40 Guarantees, bonds etc..	5,422	3.1%	6,672	3.1%	4,249	1.5%
41 Short-term self liquidating contingencies						

FSDH MERCHANT BANK LIMITED

STATEMENT OF COMPREHENSIVE INCOME	31-Dec-2020		31-Dec-2021		31-Dec-2022	
	N'millions		N'millions		N'millions	
42 Interest income	10,574	64.8%	11,069	80.3%	18,708	76.5%
43 Interest expense	(6,814)	-41.8%	(7,563)	-54.9%	(12,759)	-52.2%
44 Loan loss expense	(1,027)	-6.3%	(146)	-1.1%	(1,328)	-5.4%
45 NET REVENUE FROM FUNDS	2,733	16.8%	3,360	24.4%	4,622	18.9%
46 ALL OTHER INCOME	5,739	35.2%	2,718	19.7%	5,739	23.5%
47 NET EARNINGS	8,472	51.9%	6,078	44.1%	10,361	42.4%
48 Staff costs	(2,137)	-13.1%	(2,227)	-16.2%	(2,655)	-10.9%
49 Depreciation expense	(525)	-3.2%	(444)	-3.2%	(337)	-1.4%
50 Other operating expenses	(2,165)	-13.3%	(2,399)	-17.4%	(3,316)	-13.6%
51 TOTAL OPERATING EXPENSES	(4,827)	-29.6%	(5,071)	-36.8%	(6,308)	-25.8%
52 PROFIT (LOSS) BEFORE TAXATION	3,645	22.3%	1,007	7.3%	4,053	16.6%
53 TAX (EXPENSE) BENEFIT	(367)	-2.3%	(120)	-0.9%	(493)	-2.0%
54 PROFIT (LOSS) AFTER TAXATION	3,277	20.1%	887	6.4%	3,560	14.6%
55 NON-RECURRING INCOME (EXPENSE) - NET						
56 PROPOSED DIVIDEND	(2,001)	-12.3%	(719)	-5.2%	(2,268)	-9.3%
57 GROSS EARNINGS	16,313	100%	13,787	100%	24,447	100%
58 AUDITORS	PWC		PWC		PWC	
59 OPINION	CLEAN		CLEAN		CLEAN	

KEY RATIOS	31-Dec-2020	31-Dec-2021	31-Dec-2022
EARNINGS			
60 Net interest margin	35.6%	31.7%	31.8%
61 Loan loss expense/Interest income	9.7%	1.3%	7.1%
62 Return on average assets (Pre - tax)	2.1%	0.5%	1.6%
63 Return on average equity (Pre - tax)	13.3%	3.6%	14.0%
64 Operating Expenses/Net earnings	57.0%	83.4%	60.9%
65 Gross earnings/Total assets & contingents	9.4%	7.1%	9.8%
EARNINGS MIX			
66 Net revenue from funds	32.3%	55.3%	44.6%
67 All other income	67.7%	44.7%	55.4%
LIQUIDITY			
68 Total loans & leases - net/Total lcy deposits	68.1%	115.7%	145.4%
69 Liquid assets/Total lcy deposits*	36.8%	26.0%	39.3%
70 Demand deposits/Total lcy deposits	25.0%	34.0%	33.7%
71 Savings deposits/Total lcy deposits			
72 Time deposits/Total lcy deposits	50.6%	32.8%	35.0%
73 Inter-bank borrowings/Total lcy deposits	24.3%	33.2%	31.3%
74 Interest expense - banks/Interest expense	16.9%	4.9%	7.2%
75 NET FOREIGN CURRENCY ASSETS (LIABILITIES' millions)	1,262	(6,527)	(19,197)

FSDH MERCHANT BANK LIMITED
KEY RATIOS CONT'D
31-Dec-2020
31-Dec-2021
31-Dec-2022
ASSET QUALITY

76 Performing loans (N'000)	38,038,545	75,327,368	116,565,969
77 Non-performing loans (N'000)	2,275,538	3,717,349	1,997,983
78 Non-performing loans/Total loans - Gross	5.6%	4.7%	1.7%
79 Loan loss provision/Total loans - Gross	5.6%	3.1%	1.1%
80 Loan loss provision/Non-performing loans	2137.6%		
81 Risk-weighted assets/Total assets & contingents	32.4%	48.8%	57.0%

CAPITAL ADEQUACY

82 Adjusted capital/risk weighted assets	49.0%	29.8%	18.2%
83 Tier 1 capital/Adjusted capital	90%	82%	91%
84 Total loans - net/Adjusted capital	1.37	2.46	3.95
85 Capital unimpaired by losses (N'000)		25,686,579	27,267,546

CAPITAL ADEQUACY STRESS TEST

86 Total shareholders' funds (N'000)	27,790,842	31,096,468	29,657,774
87 Cumulative loan loss provision (actual reserves)	2,241,681	2,417,816	1,352,531
88 Equity before all provision (line 86 + line 87)	30,032,523	33,514,284	31,010,305
89 Required reserves*	8,036,504	13,914,933	17,002,258
90 Equity after required reserves (line 88 - line 89)	23,071,736	20,675,068	15,083,764
86 Equity after required reserves/risk weighted assets	40.6%	19.8%	9.3%

STAFF INFORMATION

87 Net earnings per staff (N'000)	68,326	49,015	70,964
88 Staff cost per employee (N'000)	17,235	17,959	18,184
89 Staff costs/Operating expenses	44.3%	43.9%	42.1%
90 Average number of employees	124	124	146
91 Average staff per branch	41	41	49

OTHER KEY INFORMATION

92 Legal lending limit(N'000)	12,723,033	12,843,290	13,633,773
93 Number of branches	3	3	3
94 Age (in years)	28	29	30
95 Government stake in equity (Indirect)	Nil	Nil	Nil

Actual
Actual
Estimate
MARKET SHARE OF INDUSTRY TOTAL

	2020	2021	2022
96 Lcy deposits (excluding interbank takings)	0.28%	0.19%	0.24%
97 Total assets & contingents	0.34%	0.34%	0.46%
98 Total loans & leases - net	0.22%	0.36%	0.55%
99 Net earnings	0.33%	0.19%	0.33%
100 Profit before tax	0.47%	0.09%	0.35%
101 Cash dividend	0.92%	0.19%	0.61%

RATING DEFINITIONS

Aaa A financial institution of the best financial condition and strongest capacity to meet obligations as and when they fall due relative to all other issuers in the same country.

<i>Aa</i>	A financial institution of very good financial condition and strong capacity to meet its obligations as and when they fall due relative to all other issuers in the same country.
<i>A</i>	A financial institution of good financial condition and strong capacity to meet its obligations relative to all other issuers in the same country.
<i>Bbb</i>	A financial institution of satisfactory financial condition and adequate capacity to meet its obligations as and when they fall due relative to all other issuers in the same country.
<i>Bb</i>	A financial institution with satisfactory financial condition but limited capacity to meet obligations as and when they fall due relative to all other issuers in the same country.
<i>B</i>	A financial institution with weak financial condition and weak capacity to meet obligations as and when they fall due relative to all other issuers in the same country.
<i>C</i>	A financial institution with very weak financial condition and very weak capacity to meet obligations as and when they fall due are relative to all other issuers in the same country.
<i>D</i>	In default.

A "+" (plus) or "-" (minus) sign may be assigned to ratings from Aa to C to reflect comparative position within the rating category. Therefore, a rating with + (plus) attached to it is a notch higher than a rating without the + (plus) sign and two notches higher than a rating with the - (minus) sign.

ESG CREDIT RATING CONTRIBUTION SCORE GUIDE

1	Environmental, Social and Governance issues do not contribute to credit risk
2	Environmental, Social and Governance issues have minimal contribution to credit risk
3	Environmental, Social and Governance issues have a material contribution to credit risk
4	Environmental, Social and Governance issues contribute significantly to credit risk
5	Environmental, Social and Governance issues have major contribution to credit risk

