Coronation Merchant Bank Limited

2020 Final Rating Report

Agusto&Co.

Research, Credit Ratings, Credit Risk Management

Coronation Merchant Bank Limited

Rating Assigned:

A+

Outlook: Stable
Issue Date: 20 May 2020
Expiry Date: 30 June 2021
Previous Rating: A+

Industry: Banking

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A financial institution of good financial condition and ability to meet its obligations as and when they fall due.

Rating Rationale

Agusto & Co. affirms the '**A+**' rating assigned to Coronation Merchant Bank Limited ('Coronation MB' or 'the Bank'). The rating reflects the Bank's leading position in the merchant banking segment, good capitalisation, nil impaired loans and good liquidity position. However, the rating is constrained by the lingering concentration in the loan book and relatively high funding costs. The rating also takes into cognition the impact of the COVID-19 pandemic, which has led to severe uncertainty surrounding the Nigerian economy.

As at 31 December 2019, Coronation MB's gross loans and advances stood at ₦72.7 billion, a marked year-on-year increase of 33.9%. Growth was upheld by an expansion in trade financing, a key lending focus. As at FYE 2019, Coronation MB did not record any loan impairments and had the entire loan book classified under stage 1. However, the concentration in the loan book lingers as the top 20 obligors accounted for 97% while two economic sectors represented 82.1% of the portfolio of loans as at FYE 2019. Thus, Coronation MB is vulnerable to deterioration in the financial condition of any of these top obligors, particularly in a period of economic downturn. Nevertheless, our concerns are somewhat moderated by the quality of obligors (largely blue-chip corporates) and the short-dated nature of the facilities.

During the year under review, Coronation MB introduced various cost management initiatives. However, relatively high funding costs constrained performance as profit before tax remained stagnant at ₦5 billion. As a result, pre-tax return on average assets (ROA) and pre-tax return on average equity (ROE) dropped to 1.7% (FY 2018: 2.5%) and 15.4% (FY 2018: 17.2%) respectively. While we consider the Bank's profitability to be satisfactory by industry standards, we believe the COVID-19 pandemic and the downward review of fees and charges by the Central Bank in January 2020, will adversely impact near-term performance.

Coronation MB's core capital grew by 6.3% to ₦33.7 billion as at FYE 2019, more than double the regulatory minimum for merchant banks operating in Nigeria. As at the same date, the Bank's capital adequacy ratio stood at 19.2% and surpassed the 10% regulatory threshold. We believe capitalisation remains good for the current level of business risk. In addition, the Bank plans to issue a bond in the tier 2 capital category, which will further support capitalisation in the short term.

In view of its limited branch network, Coronation MB improved its payments and collections infrastructure and was appointed the designated collections bank for the Nigeria Customs Service (NCS). As a result, high-cost deposits reduced slightly and accounted for 85% of customer deposits, lower than 90% in the prior year. We believe the proportion of high-cost deposits remains substantial and is a drag on performance. We expect funding costs to increase by about 100 – 200 basis points in 2020. Our expectations are hinged on higher interest rates as the sovereign increases domestic borrowings to fund the budget deficit. The planned bond issuance will also increase the cost of funding.

As at March 2020, Coronation MB had about US$310 million trade lines including a US$40 million trade finance guarantee facility obtained from the International Finance Corporation (IFC). The Bank intended five-year bond is also expected to support funding stability. Overall, we believe the Bank is adequately positioned to grow business volumes, albeit moderated by the prevailing economic conditions.

Subsequent to year-end, in February 2020, Coronation Merchant Bank Limited's pioneer Managing Director (Mr. Abubakar Jimoh) retired, effective April 2020. Successively, the erstwhile Deputy Managing Director, Mr Banjo Adegbohungbe was appointed as the Managing Director/CEO. Agusto & Co. does not anticipate material changes in the Bank's business strategy considering that newly appointed MD was a member of the Board and executive management.

Based on the aforementioned, we hereby attach a **stable** outlook to the rating of Coronation Merchant Bank Limited. Agusto & Co. will continue to monitor the rating and the outlook as the impact of COVID-19 on the operating environment evolves.

Strengths

- Good capitalisation
- Good asset quality
- Good liquidity position

Weaknesses

- Concentration in loan book and deposits- typical of merchant banks in Nigeria
- High dependence on interest rate sensitive funds

Challenges

- Growing quality risk assets and profitability as the Bank contends with prevailing macroeconomic headwinds
- Maintaining asset quality as oil shocks amplifies the vulnerability of the economy.

Table 1: Financial Information

	31 December 2018	**31 December 2019**
Total Assets & Contingents	₦255.2 billion	₦352.3 billion
Gross Loans	₦54.3 billion	₦72.7 billion
Deposit Liabilities (excluding interbank takings)	₦126.9 billion	₦138.1 billion
Net Earnings	₦10.6 billion	₦10.4 billion
Pre-tax Return on Average Assets & Contingents (ROA)	2.5%	1.7%
Pre-tax Return on Average Equity (ROE)	17.2%	15.4%

PROFILE

Coronation Merchant Bank Limited ('Coronation MB' or 'the Bank') was incorporated in 1992 as Associated Discount House Limited (ADHL), a limited liability company. ADHL obtained a discount house licence in July 1993 and commenced operations in August of the same year. Following structural changes in the financial services sector and declining customer confidence in discount houses, ADHL obtained a merchant bank licence from the Central Bank of Nigeria (CBN) in April 2015 and was renamed Coronation Merchant Bank Limited in July 2015. The transition to merchant banking prompted changes in the shareholding structure. Access Bank Plc and Wema Bank Plc (formerly significant shareholders) and Sterling Bank Plc divested from Coronation MB, due to regulations prohibiting banks from having ownership interests in other deposit money banks.

As at 31 December 2019, an individual and 13 institutional investors collectively held Coronation MB's equity. As at the same date, Wapic Insurance Plc, Marina Securities Limited, Coronation Capital (Mauritius) Limited, United Securities Limited, Regali Estate Limited and Mikeade Investment Company Limited were the significant shareholders and together controlled 80% shareholding. In 2019, the Bank divested from its erstwhile subsidiaries: Coronation Asset Management Limited and Coronation Securities Limited. The divestment was to realign the strategic focus to core banking. Coronation Asset Management was sold to Coronation Capital (Mauritius). On 30 June 2019, Coronation MB approved the distribution of the equity stake in Coronation Securities Limited to the shareholders as a dividend in specie.

Coronation Merchant Bank Limited's core business strategy focuses on trade finance, private wealth management, treasury and investment banking activities. These activities are carried out through the Bank's four business units: Corporate Banking, Investment Banking, Private Wealth and Global Markets & Treasury.

The Bank operates from three locations, the head office located at 10 Amodu Ojikutu Street, Victoria Island, Lagos and two branches in Port Harcourt, Rivers State and the Federal Capital Territory (FCT).

Correspondent Banks

As at 31 December 2019, Coronation MB had correspondent banking relationships with the following 17 banks:

1.	Access Bank Plc	9.	FBN UK Limited
2.	Access Bank UK	10.	FCMB UK Limited
3.	Africa Finance Corporation	11.	First Rand Bank
4.	Africa Export-Import Bank (AFREXIM)	12.	Guaranty Trust Bank Plc
5.	Bank of Beirut	13.	ODDO BHF
6.	British Arab Commercial Bank UK	14.	Standard Bank South Africa
7.	Commerzbank	15	United Bank for Africa (UBA) New York
8.	Crown Agent Bank	16.	Union Bank UK Limited
17.	International Finance Corporation (IFC)		

Information Technology

Coronation MB employs both hardware and software tools to support business operations. The Bank has over 20 applications including Finacle, the core banking application. The operating system is supported by Microsoft SQL server and Oracle 11g RDBMS. A Wide Area Network (WAN) Link is also deployed for uninterrupted communication between the business offices in Lagos, Abuja and Port Harcourt. Coronation MB's business transactions are routed through the Nigeria Inter-Bank Settlement System (NIBBS) switch facility. The Bank hosts an online transactional banking platform for its customers. To support business continuity, Coronation MB has three disaster recovery sites in Lagos, one serves as an alternative work site while the other two are used for data management.

Track Record of Financial Performance

Coronation MB's total assets and contingents grew by 38.1% year-on-year to stand at ₦352.3 billion as at 31 December 2019. The Bank's asset base has grown by a compounded annual growth rate of 45.4% since it commenced merchant banking operations in 2015. The loan book has also grown in a similar trend, with a CAGR of 33.7% over the same period, supported by a focus on short-dated trade finance transactions. The Bank continues to maintain a conservative lending appetite, with core focus on top-tier corporates. Coronation MB has continued to maintain a nil non-performing loan ratio. As at 31 December 2019, the Bank's shareholders' funds stood at ₦33.7 billion while capital adequacy ratio was 19.2%. However, during the year under review, pre-tax return on average assets and contingents (ROA) and pre-tax return on average equity declined to 1.7% (FY 2018: 2.5%) and 15.4% (FY 2018: 17.2%) respectively.

Directors		Direct & Indirect Shareholding %
Mr. Babatunde Folawiyo	*Chairman*	4.5%
Mr. Abubakar Jimoh*	*Managing Director/CEO*	2.1%
Mr. Banjo Adegbohungbe**	*Deputy Managing Director*	Nil
Mr. Idaere Gogo Ogan	*Non-Executive Director*	Nil
Mr. Adamu Atta	*Non-Executive Director*	Nil
Mr. Larry Ettah	*Non-Executive Director*	4.7%
Ms Evelyn Oputu	*Non-Executive Director*	Nil
Mrs. Suzanne Iroche	*Non-Executive Director - Independent*	Nil
Mr. Babatunde Dabiri	*Non-Executive Director - Independent*	Nil
Ms. Olubunmi Fayokun	*Non-Executive Director - Independent*	Nil

** Retired effective April 2020*
***Appointed Managing Director effective May 1 2020*

MANAGEMENT TEAM

Mr. Banjo Adegbohungbe was appointed Managing Director/Chief Executive Officer of Coronation Merchant Bank Limited on May 1 2020. He has over two decades of commercial banking experience spanning various roles including global trade, corporate and investment banking, operations, treasury management, strategic planning and corporate services. He commenced his banking career at Citibank Nigeria Limited and thereafter, Access Bank Plc. Mr. Adegbohungbe joined Coronation MB in June 2018 as an Executive Director/Chief Operating Officer and thereafter appointed Deputy Managing Director. He is a Mechanical Engineering graduate from Obafemi Awolowo University (OAU), Ile-Ife and holds a Master's in Business Administration from the International Institute for Management (IMD), Switzerland. Mr. Adegbohungbe is also a member of the Chartered Institute of Bankers of Nigeria (CIBN).

Other members of Coronation MB's senior management team include:

Magnus Nnoka	*Group Head, Risk Management*
Cornelia Utuk	*Head, Legal Services/Company Secretary*
Ademola Adekoya	*Group Head, Corporate Banking*
Dele Dopemu	*Chief Audit Executive*
Ibrahim Bello	*Chief Compliance Officer*
Chukwukadibia Okoye	*Chief Financial Officer*
Iyobosa Sorae	*Head, Treasury and Global Markets*
Eshiovaze Momoh	*Chief Technology Officer*
Akinyemi Oluwadare	*Head, Group Operations*
Ayodele Odufuye	*Head, Human Resources*
Aderemi Makinde	*Head, Projects, Facilities Management and Administration*

ANALYSTS' COMMENTS

ASSET QUALITY

As at 31 December 2019, Coronation Merchant Bank Limited's total assets and contingents amounted to ₦352.3 billion, representing a 38.1% year-on-year growth. The increase was upheld by an expanded pool of deposit liabilities and inter-bank takings. The growth was most prominent in contingents, comprising guarantees and letters of credit, which rose by 205.7% to ₦99 billion and represented 28.1% of the asset base. Coronation MB's loan book grew by 33.9% to ₦72.7 billion, largely due to higher trade finance solutions, which forms the core of the Bank's lending strategy. Gross loans and advances accounted for 20.6% of total assets and contingents as at 31 December 2019. We also attribute the traction in lending activities to the introduction of the minimum loan-to-deposit ratio (LDR) policy by the CBN.

Coronation MB's lending strategy largely focuses on blue-chip corporates in various key sectors. The Bank provides a host of financial services including international trade finance and working capital solutions to these businesses. The bulk of these facilities are short-tenured, as evidenced by 99% of the loan book maturing within 6 months. Despite a 28% growth in foreign currency (FCY) loans, the loan book remains skewed to local currency loans. As at FYE 2019, local currency denominated loans accounted for 57% of gross loans and advances (FYE 2018: 55%). FCY loans are typically short-dated loans relating to international trade transactions. These loans are collateralised by corporate guarantees, all asset debentures, real estate and other permissible means.

Figure 1: Sectorial Breakdown of the Loan Book (FYE 2019)

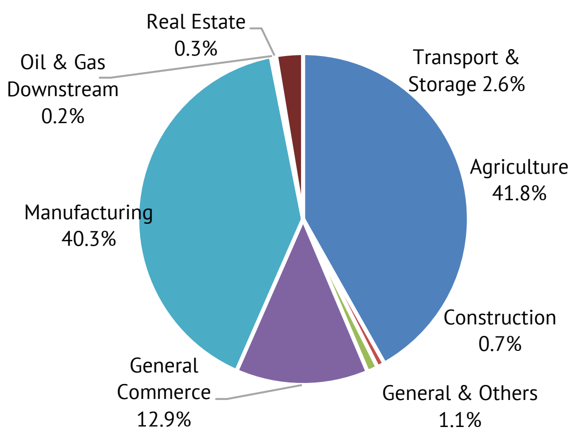
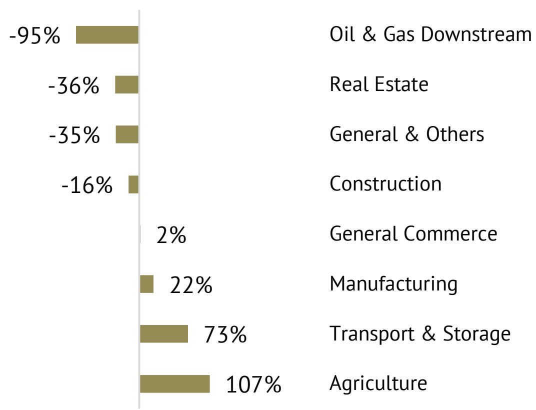


Figure 2: Loan Growth by Sector (FYE 2019)



A breakdown of the loan book indicates that the highest growth was recorded in loans granted to obligors in the agriculture sector, where credit exposures spiked by 107% to ₦30.4 billion. This accounted for 41.8% of the loan book, which we consider to be high. Loans to these obligors are typically to finance export activities, which we view positively. However, due to supply chain interferences elicited by COVID-19, the relatively high exposure subjects the loan book to the sector's adversities. There is also a high concentration in the manufacturing sector, which accounted for 40.3% of gross loans and advances as at FYE 2019. While these loans are to a cluster of top-tier companies in various industries with different business fundamentals, we believe the land border closure and the COVID-19 pandemic has adversely impacted these businesses. Given that these companies rely heavily on imported inputs, the devaluation of the naira could further constrain the performance of these obligors. Nevertheless, the Bank's management has disclosed that about 44% of trade finance facilities are for local orders, which should moderate the impact of the anticipated naira devaluation beyond the 5.3% recorded in March 2020. Coronation MB seeks to diversify the loan book by lending to critical sectors such as utilities and services. However, in view of the prevailing macroeconomic headwinds, which we believe will constrain growth, we expect the loan book to remain concentrated in the near-term.

The obligor concentration in the loan book lingers. Coronation MB's top 20 borrowing customers, accounted for 97% of gross loans while the largest credit exposure represented 37% of the Bank's shareholders' equity as at FYE 2019. Thus, increasing the Bank's susceptibility to a deterioration in the financial condition of any of these obligors. The bulk of these credit facilities are short-dated and typically have multiple lending cycles in a year, backed by adequate collateral. Therefore, our concerns are moderated to an extent.

As at FYE 2019, Coronation MB had no impaired loans with all credit exposures deemed to have very low default risk, categorised under stage 1. This is similar to its selected peers, Nova Merchant Bank Limited ('Nova MB') and Rand Merchant Bank Limited ('Rand MB'). Despite maintaining a nil impaired credit position since inception, the Bank makes annual provisions for potential credit losses in line with CBN prudential guidelines. As at FYE 2019, the Bank had cumulative loan loss provisions of ₦58.3 million, in addition to regulatory risk reserves of ₦2.5 billion, which is expected to moderate losses should a credit event occur. We believe the Bank's focus on low-risk top corporates as well as its risk management framework continues to uphold asset quality.

In our opinion, Coronation MB's asset quality is good. Nevertheless, we believe the Bank will contend with macroeconomic headwinds, which points at a likely recession and therefore will require stringent risk measures to forestall loan losses. We also believe that the global pandemic and the plan by the CBN to ensure that merchant banks focus on supporting the real sector with long-dated loans will test the Bank's lending strategy, which primarily focuses on short-term trade solutions.

RISK MANAGEMENT

Coronation Merchant Bank Limited maintains a centralised risk management infrastructure, with the risk appetite and governance defined by the Board of Directors (BoD). The Bank's risk appetite is defined as moderate, reflected in limits and thresholds outlined in the operating policies and procedures, which cuts across all Coronation MB's business lines. The BoD provides this oversight function through the Board Risk Management and the Board Credit and Investment Committee, chaired by Non-Executive Directors. Supporting the BoD's functions are three management committees – the Asset and Liability Management Committee

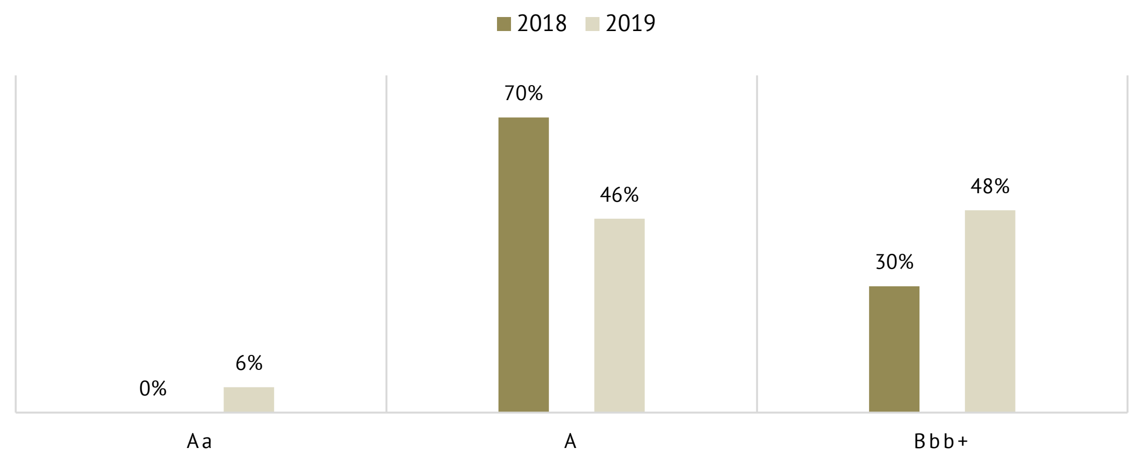
(ALCO), the Enterprise Risk Management Committee (ERMC) and the Management Credit & Investment Committee (MCIC).

The Bank has an independent risk management function, overseen by the Chief Risk Officer (CRO), who is responsible for maintaining and implementing the appropriate risk culture. Coronation MB's risk management function is split into two departments: the Credit Risk department and the Enterprise Risk Management department (which oversees market and operational risk).

Credit Risk

Coronation MB is exposed to credit risk largely from its loan book and investments in debt securities. The Bank adopts a minimum acceptable risk rating of '**Bbb+**' for its counterparties, estimated via an internal risk rating model. This approaches credit risk ratings through two perspectives: Obligor Risk Rating (ORR) and Facility Risk Rating (FRR). Coronation MB adopts a rating scale with 22 risk categories ranging from Aaa (lowest level of credit risk) to D (lost). As at 31 December 2019, the Bank only had loans in the Bbb+ (48%), A (46%) and Aa (6%) rating categories.

Figure 3: Credit Quality of the Loan Book (FYE 2019)



Coronation Merchant Bank Limited's lending policy mandates the collateralisation of all credit exposures. Acceptable collateral includes cash deposits, equity securities, pledge goods, legal mortgage, bankers' acceptance and shipping documents. As at FYE 2019, 78% of the loan book was collateralised, while a large bulk of the loans are self-liquidating in nature. The Bank's exposures are also backed as trust receipts and negative pledges.

Market Risk

Exposure to market risk in the Bank's trading and non-trading portfolio emanates from changes in interest rates, exchange rates and equity prices. The Bank minimises exposure to market risk by setting defined limits such as gap limits, deposit concentration limits and stop-loss limits. Daily mark-to-market valuation of positions held in the trading book is also conducted to moderate market risk exposures within acceptable thresholds. Other key market risk management measures adopted by the Bank include a gap analysis for interest rate sensitivity and stress tests to ascertain the level of potential losses that could arise in extreme economic conditions. A sensitivity of the Bank's profit to a 10% naira devaluation results in a ₦1.3 billion gain.

Operational Risk

Coronation MB retains the use of the Basic Indicator Approach for measuring operational risk. This is supported by a five-tier risk matrix, which assesses the likelihood of a risk occurrence vis-à-vis the financial impact to the Bank.

In 2019, the Bank paid a total of ₦375,000 (a 66.6% year-on-year decline) as penalties for the late submission of regulatory filings. Coronation MB's number of customer complaints increased to 42 (FY 2018: 15) largely due to increased number of complaints from the internet banking platform. Attributable to a higher discrepancy in accrued interest, the Bank refunded a total of ₦39 million to customers, a 145% increase over the prior year.

In our opinion, Coronation Merchant Bank's risk management framework is adequate for the current level of business risk. However, we believe that additional improvements are required in the Bank's internal processes to forestall a further increase in operational errors and customer complaints.

EARNINGS

Coronation Merchant Bank Limited generates income from lending activities, securities trading and investment banking. The capabilities established from the discount house antecedence has supported treasury activities, which has steadily accounted for an average 40% of the Bank's earnings.

Despite the expansion in the loan book and a marked improvement in ancillary income in 2019, the Coronation MB's net earnings reduced marginally by 2% to ₦10.4 billion. Earnings were impacted by relatively high funding costs and subdued income from lending – given the Bank's focus on the top-tier corporates, who are typically more interest-rate sensitive. Thus, interest income increased moderately by 3% to ₦25.1 billion. During the review period, interest expense increased by 19.5% to ₦20.7 billion, as a result of the Bank's reliance on costly funding. Thus, the Bank's net interest spread (NIS) decreased to 17.6%, lower than 28.8% in FY 2018, Nova MB's 48.3% and Rand MB's 38.6%. Coronation MB's NIS has maintained a downward trajectory since 2016. In the near-term, we do not anticipate a material improvement in NIS, in view of the high competition in the corporate lending space. We also expect an uptick in interest expense particularly in the second half of 2020 as the government increases local debt offerings to fund its budget and the Bank's planned bond costs reflects.

The Bank made provisions of ₦90.5 million for potential losses from the loan book and other financial assets. The provisions, which were largely due to the allowance for potential losses from placements with financial institutions, remained marginal and accounted for 0.4% of interest income.

Figure 4: Contributors to Interest Income (FY 2017 – FY 2019)

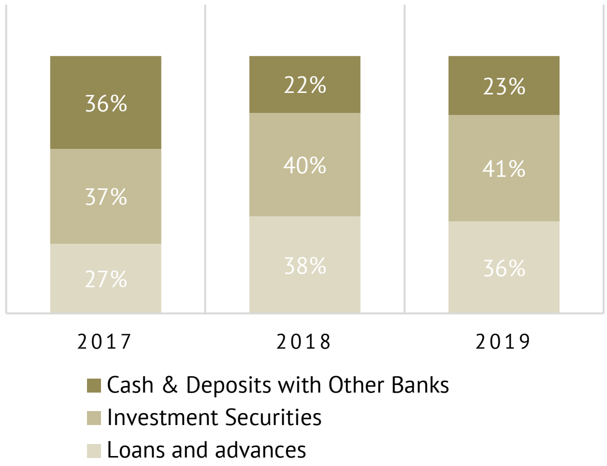
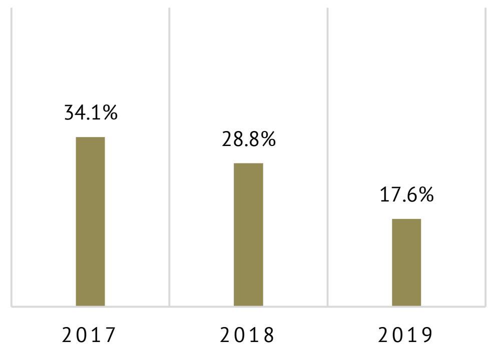
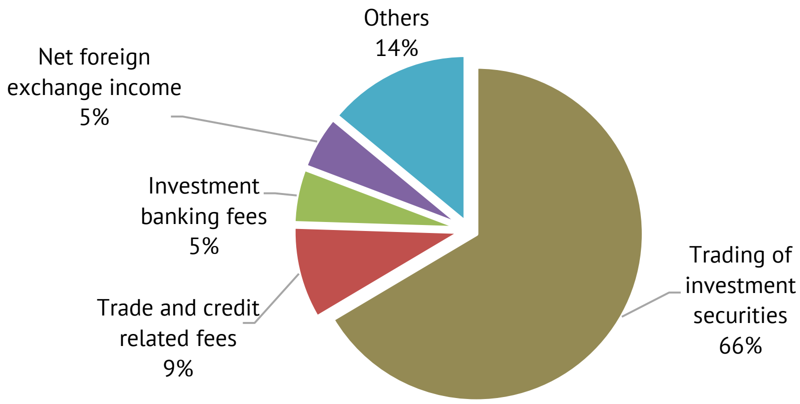


Figure 5: Net Interest Spread (FY 2017 – FY 2019)



During the financial year ended 31 December 2019, non-interest income grew by 64.4% to ₦6 billion. Securities trading remains a significant contributor to earnings, reflecting a relatively strong treasury function established from the discount house antecedence. The Bank recorded a 141.5% spike in net gains on investment securities to ₦4 billion, elicited by the favourable impact of the low interest rate environment on fixed-income securities pricing in the last quarter of the year. Coronation MB also benefitted from a 173.2% increase in net income from foreign exchange activities (trading and revaluation gains). Driven by FCY dividends, income from equity securities jumped by 225.3% to ₦304.3 million. However, the Bank recorded a decline in credit-related and investment banking fees. The dip in investment banking income was due to one-off fees earned in the prior year. The prevailing fragile macroeconomy creates avenue for a higher need for financial advisory services, particularly corporate restructuring, mergers and acquisitions. Therefore, we expect Coronation MB's investment banking income to improve in 2020. Nevertheless, with the CBN's downward review of bank charges in January 2020 and the anticipated drop in credit-related fees, due to expected marginal loan growth, non-interest income will moderate in 2020.

Figure 6: Breakdown of Non-Interest Income in FY 2019

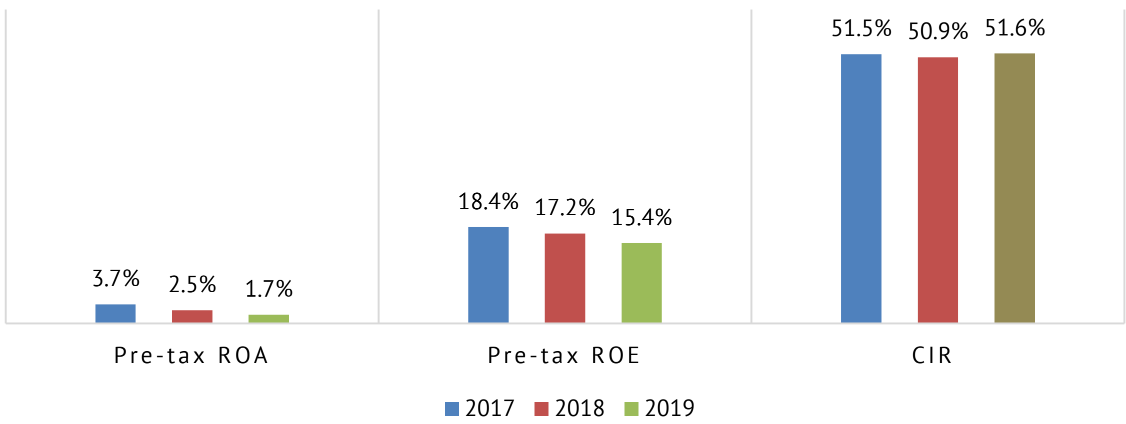


Coronation Merchant Bank embarked on cost optimisation initiatives in 2019. Despite rising inflationary trends, the Bank's initiatives recorded some success as operating expenses (OPEX) stood at par with the prior year at ₦5.3 billion. However, due to muted earnings, the Bank's cost-to-income ratio (CIR) increased marginally by 70 basis points to 51.6%, higher than Rand MB's 31% but lower than Nova MB's 55.3% and the banking industry average of 65.9%. While we expect the Bank to sustain cost optimisation measures, we believe that inflationary pressures coupled with devaluation of the naira will dampen the success of the exercise in the near term. Thus, we expect a higher CIR in 2020.

In FY 2019, Coronation MB's profit before tax stood at ₦5 billion, largely due to the increase in interest expense, which moderated net earnings. Consequently, pre-tax return on average assets and contingents (ROA) declined to 1.7% (2018: 2.5%) while pre-tax return on average equity (ROE) dropped to 15.4% (2018: 17.2%). The Bank's pre-tax ROE was lower than the estimated banking industry average of 22.9%, Rand MB's 35.8%. However, it was higher than Nova MB's 8.2% and the 13.9% average yield on 364-day treasury certificate in the same period.

Subsequent to year-end, in Q1 2020, the Bank's profitability indicators dipped further with annualised pre-tax ROA and pre-tax ROE of 0.9% and 10.7% respectively. CIR also increased to 64.1% during the period. In our opinion, with the increase in the applicable cash reserve ratio (CRR) for merchant banks to 27.5% from 2% and the anticipated increase in operating expenses, the Bank's near-term profitability will remain satisfactory by industry standards.

Figure 7: Profitability Indicators (2017 – 2019)



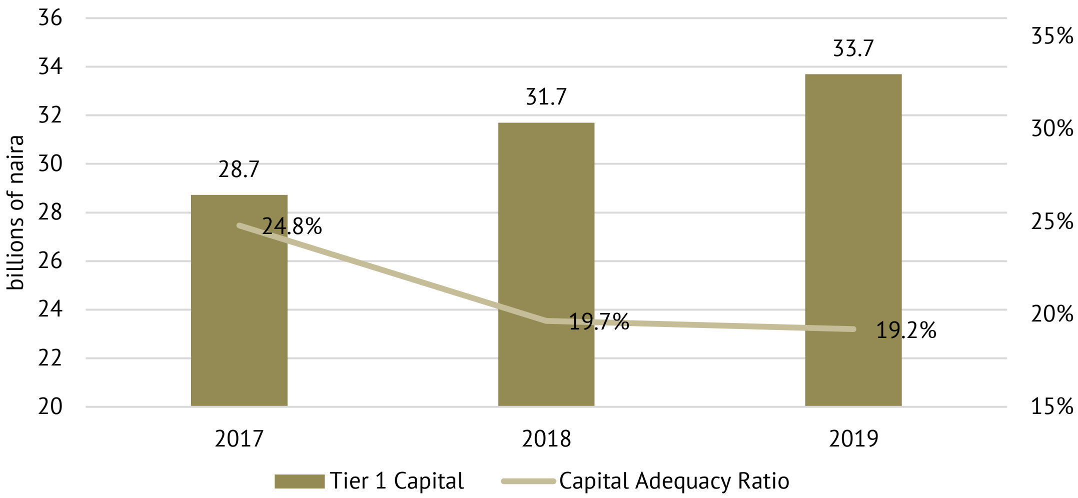
CAPITAL ADEQUACY

As at 31 December 2019, Coronation Merchant Bank Limited's tier 1 (core) capital increased by 6.3% year-on-year to ₦33.7 billion and funded 9.6% of total assets and contingents. At this level, Coronation MB's core capital is more than double the ₦15 billion regulatory minimum for merchant banks operating in Nigeria. The moderate growth in core capital was supported by an increase in the appropriation to non-distributable reserves amidst muted growth in earnings. Revenue reserves declined by 88.1% to ₦183.4 million, due to distributions of ₦1.4 billion to shareholders emanating from the disposal of Coronation Securities Limited, one of its erstwhile subsidiaries. Tier 2 capital, which comprises fair value reserves stood at ₦870.4 million from a negative of ₦545.3 million in 2018.

Due to an increase in risk-weighted assets elicited by the expanded loan book, the Bank's capital adequacy ratio (CAR), decreased slightly to 19.2% from 19.7% recorded in the prior year and lower than the selected peers: Nova MB (54.3%) and Rand MB (50.1%). Nevertheless, Coronation MB's CAR remained well above the regulatory minimum of 10% for merchant banks. The Bank intends to issue a medium-term bond in the tier 2 capital category, which will further uphold capitalisation.

In our opinion, the Bank's capitalisation is good for the level of business risk undertaken. In the event that the CBN proceeds with recapitalisation plans for banks, we believe the Bank's shareholders will provide the required capital.

Figure 8: Tier 1 Capital and Capital Adequacy Ratio (FYE2017 – FYE2019)



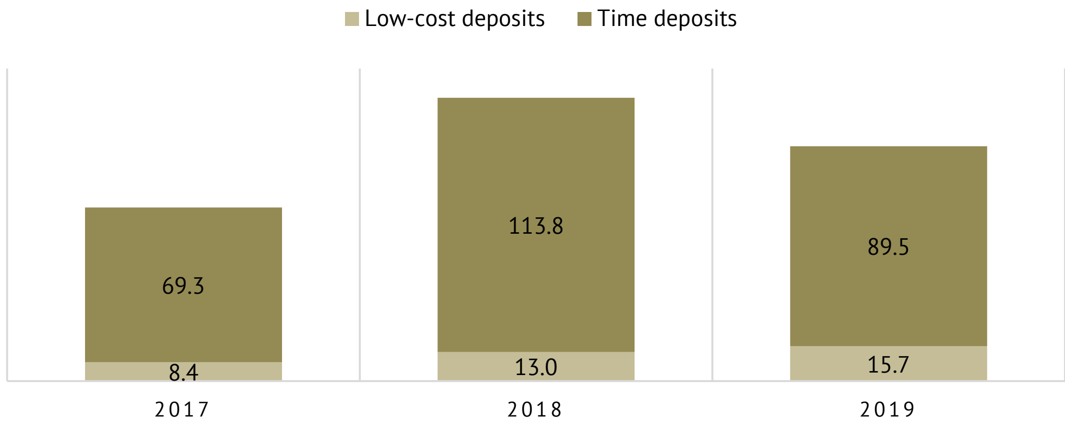
LIQUIDITY AND LIABILITY GENERATION

Coronation Merchant Bank Limited is primarily funded by liabilities generated from customers, the interbank market, commercial papers and borrowings. The Bank has also leveraged the affiliation with Coronation Asset Management Limited (the erstwhile subsidiary) to source deposits. However, given that the merchant banking model limits minimum deposits to ₦50 million per tranche, the Bank is restricted to wholesale deposits, which are typically expensive. In efforts to grow low-cost deposits, Coronation MB has improved its payments and collections infrastructure and was recently appointed the designated collections bank for the Nigeria Customs Service (NCS).

As at FYE 2019, Coronation MB had total local currency (LCY) deposits (excluding inter-bank takings) of ₦105.2 billion, a 17% year-on-year decline. The Bank's deposit mix is largely skewed towards costly tenured deposits accounting for 85% of LCY deposits. This has continually impacted the Bank's margins. Coronation MB's deposit base is also concentrated by source as the top 20 depositors contributed a high 79% of total deposits. Due to the limitations in growing substantial low-cost deposits, we expect the deposit base to remain concentrated and skewed to high-cost funds.

Supporting the growth in lending activities, largely trade finance facilities, were foreign currency (FCY) deposits, which jumped 517 times to ₦32.8 billion and funded 9.3% of total assets and contingents as at FYE 2019. FCY deposits adequately funded 105.2% of foreign currency loans. The growth in FCY deposits was largely due to additional liability products targeted at customers seeking to hedge against currency risk. Consequently, we expect a further growth in FCY deposits as customers anticipate a further naira devaluation in the near term.

Figure 9: Local Currency Deposit Liabilities (Excluding Inter-bank Takings)

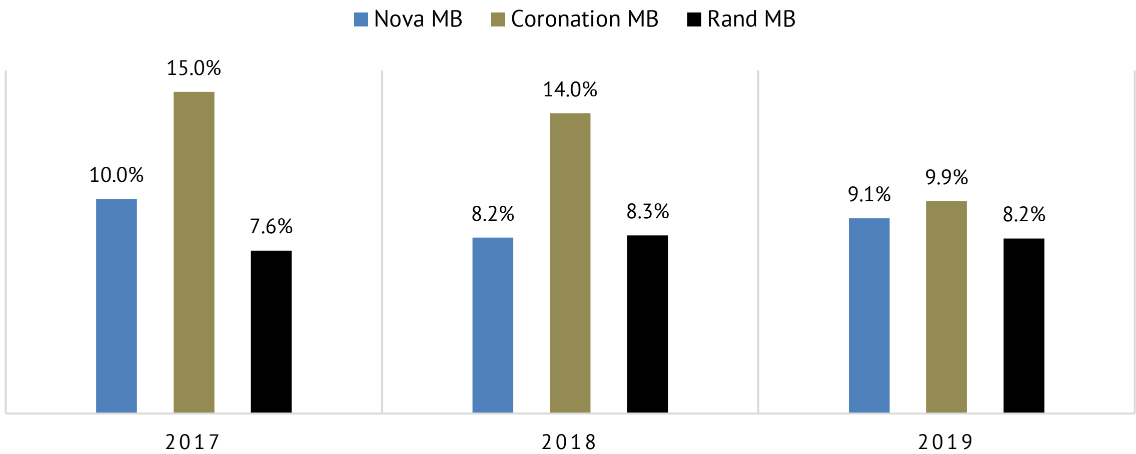


Coronation MB's inter-bank takings grew by 113.7% to ₦25.9 billion and funded 7.4% (FYE 2018: 4.8%) of total assets and contingents as at FYE 2019. This reflects a substantial reliance on the inter-bank as the associated interest expense accounted for a high 74.9% of the Bank's total interest expense (FY 2018: 57.2%). However, in a period of adverse liquidity in the system, access to the same level of substantial funding may be constrained in the near term.

During the review period, Coronation MB issued commercial papers amounting to ₦13.1 billion, reflecting a year-on-year decline of 34.3%. The commercial papers were issued in two tranches at an average interest rate of 14.3% and the outstanding balance stood at ₦12.6 billion as at FYE 2019. The Bank currently has trade lines in excess of US$300 million including the International Finance Corporation (IFC) trade finance guarantee facility consummated in March 2020. There is also a contingent funding line of about ₦5 billion with a commercial bank. The Bank intends to issue a medium-term bond in Q2 2020 to ensure a more stable funding base.

Despite the high reliance on costly funds, Coronation MB's weighted average cost of funds (WACF) reduced by 410 basis points to 9.9% in 2019. However, the Bank's WACF was the highest amongst its peers: Nova MB (9.1%) and Rand MB (8.2%), during the same period. Due to the CRR increase subsequent to year-end, the Bank prioritised funding sources excluded from the cash reserves computation. Additional commercial papers amounting to ₦23.16 billion were issued in Q1 2020 at average interest rate of 6.6%. Interbank takings, which attracted relatively low interest rates in Q1 2020, grew by 21% to ₦31.4 billion as at 31 March 2020. Consequently, WACF further improved to 6.2% in Q1 2020 also upheld by the prevailing low interest rate regime. However, we expect the proposed bond issuance and higher sovereign debt offerings in H2 2020 to increase funding costs.

Figure 10: Weighted Average Cost of Funds (FY 2017 – FY 2019)



The Bank's liquidity ratio (liquid assets to LCY deposits) stood strong at 102.6% as at 31 December 2019 (FYE 2018: 87.2%) and higher than the regulatory benchmark of 20% for merchant banks.

In our opinion, Coronation Merchant Bank's liquidity position is strong while we consider its ability to refinance to be adequate.

OWNERSHIP, MANAGEMENT & STAFF

As at the financial year ended 31 December 2019, Coronation Merchant Bank Limited's shareholding remained largely unchanged from the prior year. As at FYE 2019, the Bank's 5.1 billion issued shares were held by 14 shareholders: one individual and thirteen (13) institutional investors. As at the same date, the Bank had six shareholders with equity stake above 5% and these investors collectively held a substantial 80% of the Bank's equity.

Table 2: Substantial Shareholding Interests

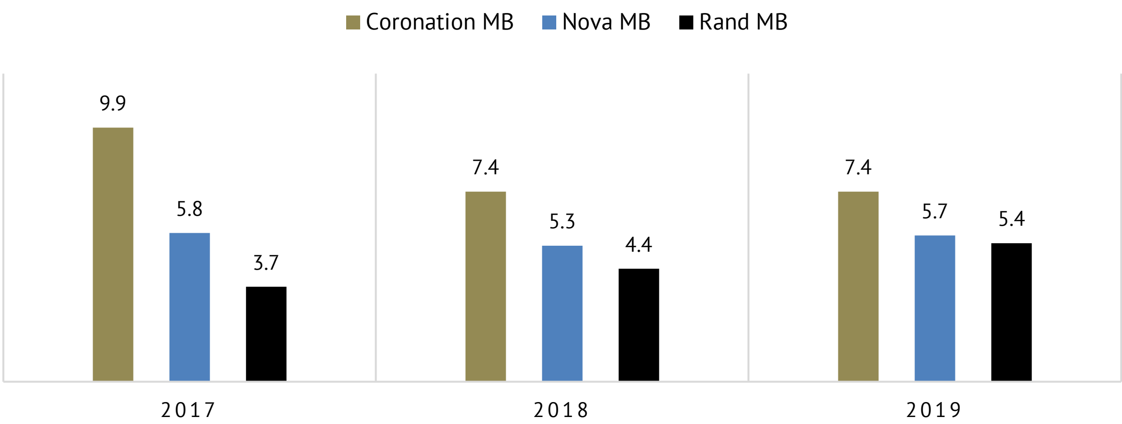
Shareholder	% of Shareholding
WAPIC Insurance Plc	22.8%
Marina Securities Limited	22.7%
Coronation Capital (Mauritius) Limited	13.3%
United Securities Limited	8.1%
Regali Estates Limited	7.5%
Mikeade Investment Co Limited	5.6%
Total	**80%**

As at 31 December 2019, the Bank was governed by a 10-member Board of Directors comprising eight Non-Executive Directors (including three Independent Non-Executive Directors) and two Executive Directors. Subsequent to the year end, in February 2020, Mr Abubakar Jimoh (the Managing Director) proceeded on terminal leave and his retirement took effect in April 2020. Subsequently, Mr Banjo Adegbohungbe, (the erstwhile Deputy Managing Director) was appointed Managing Director. We also do not anticipate a significant change in business strategy considering that the newly appointed Managing Director has been a member of the Board and executive management team. The Bank has disclosed that there will be some additional governance changes in the near term.

The Board of Directors exercises oversight functions through four standing committees: Board Risk Management Committee, Board Governance and Nominations Committee, Board Audit Committee and the Board Credit and Investment Committee. Various management committees including the Asset and Liability Management Committee (ALCO) and the Enterprise Risk Management Committee (ERMC), support the Board's oversight functions.

In 2019, Coronation MB employed an average of 121 persons, down from 125 persons in the prior year. The Bank's workforce comprised 12% management staff and 88% non-management personnel. In spite of the decline in net earnings, the marginal decline in the workforce enabled a slight improvement in staff productivity, measured by net earnings per staff, which increased to ₦85.7 million in 2019. Net earnings per staff sufficiently covered average cost per employee 7.4 times (FY 2018: 7.4 times), significantly higher than the industry average of 4.4 times, Nova MB's 5.7 times and Rand MB's 5.4 times. In our opinion, staff productivity is very good and we also consider the management team to be experienced and competent.

Figure 11: Net Earnings to Staff Cost (FY 2017 – FY 2019)



MARKET SHARE

The merchant banking segment accounts for a marginal 2% of the Industry's total assets, gross loans and deposit liabilities. This is attributable to relatively low accessibility to retail funding, in comparison to commercial banks. The merchant banks focus on corporate lending, treasury, investment banking and financial advisory.

Coronation MB is one of the three erstwhile discount houses that converted to merchant banking in 2015. With total assets and contingents of ₦352.3 billion as at FYE 2019, Coronation MB is the highest ranked merchant bank on this basis. During the review period, the Bank recorded an improvement across some market share indicators. However, this remained marginal considering the merchant banking's low contribution to the banking industry. Nevertheless, upheld by its niche in treasury and trade finance solutions, we expect Coronation MB will retain its good ranking amongst its peers.

Table 3: Market Share Indicators

	Coronation MB 2018	Coronation MB 2019	Nova MB 2019	Rand MB 2019
LCY Deposits	0.79%	0.54%	0.21%	0.16%
Total Assets and Contingents	0.67%	0.80%	0.22%	0.33%
Total Loans and Advances (Net)	0.43%	0.46%	0.18%	0.31%
Net Earnings	0.46%	0.38%	0.13%	0.88%
Pre-tax Profit	0.67%	0.54%	0.16%	1.78%

OUTLOOK

Following the divestment of the erstwhile subsidiaries, Coronation Merchant Bank seeks to grow into a more established 'Trade-Finance Investment Bank'. Supporting this will be a focus on trade financing, underpinned by strategic partnerships with key international trade enablers. The Global Markets and Treasury business line is also expected to sustain earnings, leveraging the discount house antecedence. However, some challenges persist. Due to limitations to wholesale funds, the cost of funding is expected to remain high, restricting considerable growth in profitability. The Bank's operations are also impacted by adverse regulations, most recently the revision of the cash reserve requirements to 27.5% from 2%, which may pose funding challenges. Therefore, the Bank's five-year bond issuance is expected to provide some funding stability and adequate capital buffers.

In 2020, the business environment ventured into an uncharted territory, with economic slowdown elicited by COVID-19 pandemic and the resulting glut in the global crude oil market. We anticipate asset quality pressures while earnings will be constrained for the banking industry. With the upward trend in inflation, the Bank's recent success in curtailing costs may weaken. However, with relatively good capitalisation level, Coronation MB's capitalisation ratios should remain adequate. The comparatively low risk appetite as evidenced by lending to top-tier companies in critical sectors, should uphold a healthy loan book. Nonetheless, we believe that more stringent lending conditions will be required to sustain asset quality, particularly with the adverse financial condition being faced by most businesses and households.

Based on the aforementioned, we hereby attach a **stable** outlook to the rating of Coronation Merchant Bank Limited. The outlook is hinged on our expectations that asset quality will remain satisfactory, while an adequate capitalisation will be maintained. Although we believe profitability will be impacted by the fragile business environment, we expect it to remain acceptable by industry standards. We shall continue to monitor the rating outlook as the impact of COVID-19 on the operating environment evolves.

FINANCIAL SUMMARY

CORONATION MERCHANT BANK LIMITED

	STATEMENT OF FINANCIAL POSITION AS AT	31-Dec-2019		31-Dec-2018		31-Dec-2017	
		₦'000		₦'000		₦'000	
	ASSETS						
1	Cash & equivalents	8,956,378	2.5%	3,211,035	1.3%	3,256,498	2.0%
2	Government securities	67,425,509	19.1%	82,550,611	32.4%	44,589,344	27.4%
3	Special treasury bills					29,509,041	18.1%
4	Quoted investments	47,529	0.0%	63,637	0.0%	95,021	0.1%
5	Placements with discount houses						
6	LIQUID ASSETS	76,429,416	21.7%	85,825,283	33.6%	77,449,904	47.6%
7	BALANCES WITH NIGERIAN BANKS	17,560,844	5.0%	36,905,586	14.5%	4,931,504	3.0%
8	BALANCES WITH BANKS OUTSIDE NIGERIA	39,913,047	11.3%	8,970	0.0%		
9	Direct loans and advances - Gross	72,742,231	20.6%	54,340,867	21.3%	32,247,778	19.8%
10	Less: Cumulative loan loss provision	(58,282)	0.0%	(28,408)	0.0%	(8,193)	0.0%
11	Direct loans & advances - net	72,683,949	20.6%	54,312,459	21.3%	32,239,585	19.8%
12	Advances under finance leases - net						
13	TOTAL LOANS & LEASES - NET	72,683,949	20.6%	54,312,459	21.3%	32,239,585	19.8%
14	INTEREST RECEIVABLE						
15	OTHER ASSETS	4,397,231	1.2%	2,657,644	1.0%	4,115,519	2.5%
16	DEFERRED LOSSES	5,777,715	1.6%	4,998,887	2.0%	5,203,887	3.2%
17	RESTRICTED FUNDS	8,757,976	2.5%	5,188,052	2.0%	2,300,438	1.4%
18	UNCONSOLIDATED SUBSIDIARIES & ASSOCIATES			4,614,711	1.8%	4,614,711	2.8%
19	OTHER LONG-TERM INVESTMENTS	20,651,566	5.9%	24,670,502	9.7%	3,196,055	2.0%
20	FIXED ASSETS & INTANGIBLES	7,178,645	2.0%	3,596,755	1.4%	3,621,833	2.2%
21	**TOTAL ASSETS**	**253,350,389**	**71.9%**	**222,778,849**	**87.3%**	**137,673,436**	**84.6%**
22	TOTAL CONTINGENT ASSETS	98,996,446	28.1%	32,382,378	12.7%	24,975,667	15.4%
23	**TOTAL ASSETS & CONTINGENTS**	**352,346,835**	**100%**	**255,161,227**	**100%**	**162,649,103**	**100%**
	CAPITAL & LIABILITIES						
24	TIER 1 CAPITAL (CORE CAPITAL)	33,698,683	9.6%	31,693,532	12.4%	28,726,932	17.7%
25	TIER 2 CAPITAL	870,146	0.2%	(545,267)	-0.2%	466,220	0.3%
26	Medium to long-term borrowings	12,610,440	3.6%	18,053,345	7.1%		
27	Demand deposits	15,730,463	4.5%	13,034,480	5.1%	7,061,464	4.3%
28	Savings deposits						
29	Time deposits	89,509,438	25.4%	113,804,855	44.6%	65,752,852	40.4%
30	Inter-bank takings	25,978,923	7.4%	12,159,545	4.8%	11,206,114	6.9%
31	TOTAL DEPOSIT LIABILITIES - LCY	131,218,824	37.2%	138,998,880	54.5%	84,020,430	51.7%
32	Customers' foreign currency balances	32,847,991	9.3%	57,532	0.0%	4,952,292	3.0%
33	TOTAL DEPOSIT LIABILITIES	164,066,815	46.6%	139,056,412	54.5%	88,972,722	54.7%
34	INTEREST PAYABLE						
35	OTHER LIABILITIES	42,104,305	11.9%	34,520,827	13.5%	19,507,562	12.0%
36	**TOTAL CAPITAL & LIABILITIES**	**253,350,389**	**71.9%**	**222,778,849**	**87.3%**	**137,673,436**	**84.6%**
37	TOTAL CONTINGENT LIABILITIES	98,996,446	28.1%	32,382,378	12.7%	24,975,667	15.4%
38	**TOTAL CAPITAL, LIABILITIES & CONTINGENTS**	**352,346,835**	**100%**	**255,161,227**	**100%**	**162,649,103**	**100%**
	BREAKDOWN OF CONTINGENTS						
39	Acceptances & direct credit substitutes	89,014,318	25.3%	31,759,378	12.4%	20,913,167	12.9%
40	Guarantees, bonds etc..	9,982,128	2.8%	623,000	0	4,062,500	2.5%
41	Short-term self liquidating contingencies						

CORONATION MERCHANT BANK LIMITED

	STATEMENT OF COMPREHENSIVE INCOME	31-Dec-2019 N'000		31-Dec-2018 N'000		31-Dec-2017 N'000	
42	Interest income	25,093,015	80.6%	24,286,820	86.9%	22,195,656	89.7%
43	Interest expense	(20,664,692)	-66.4%	(17,291,460)	-61.8%	(14,633,478)	-59.1%
44	Loan loss expense	(90,521)	-0.3%	(85,559)	-0.3%	51,596	0.2%
45	NET REVENUE FROM FUNDS	4,337,802	13.9%	6,909,801	24.7%	7,613,774	30.8%
46	ALL OTHER INCOME	6,035,800	19.4%	3,670,580	13.1%	2,553,116	10.3%
47	**NET EARNINGS**	**10,373,602**	**33.3%**	**10,580,381**	**37.8%**	**10,166,890**	**41.1%**
48	Staff costs	(1,404,905)	-4.5%	(1,433,036)	-5.1%	(1,031,759)	-4.2%
49	Depreciation expense	(615,692)	-2.0%	(592,516)	-2.1%	(347,985)	-1.4%
50	Other operating expenses	(3,329,121)	-10.7%	(3,359,082)	-12.0%	(3,854,317)	-15.6%
51	TOTAL OPERATING EXPENSES	(5,349,718)	-17.2%	(5,384,634)	-19.3%	(5,234,061)	-21.1%
52	PROFIT (LOSS) BEFORE TAXATION	5,023,884	16.1%	5,195,747	18.6%	4,932,829	19.9%
53	TAX (EXPENSE) BENEFIT	(257,172)	-0.8%	(711,375)	-2.5%	(314,433)	-1.3%
54	**PROFIT (LOSS) AFTER TAXATION**	**4,766,712**	**15.3%**	**4,484,372**	**16.0%**	**4,618,396**	**18.7%**
55	NON-RECURRING INCOME (EXPENSE) - NET						
56	PROPOSED DIVIDEND	(3,092,680)	-9.9%	(1,515,164)	-5.4%	(757,582)	-3.1%
57	**GROSS EARNINGS**	**31,128,815**	**100%**	**27,957,400**	**100%**	**24,748,772**	**100%**
58	AUDITORS	PWC		PWC		PWC	
59	OPINION	CLEAN		CLEAN		CLEAN	

	KEY RATIOS	31-Dec-2019	31-Dec-2018	31-Dec-2017
	EARNINGS			
60	Net interest margin	17.6%	28.8%	34.1%
61	Loan loss expense/Interest income	0.4%	0.4%	
62	Return on average assets (Pre - tax)	1.7%	2.5%	3.7%
63	Return on average equity (Pre - tax)	15.4%	17.2%	18.4%
64	Operating Expenses/Net earnings	51.6%	50.9%	51.5%
65	Gross earnings/Total assets&contingents-avg.	10.2%	13.4%	18.4%
	EARNINGS MIX			
66	Net revenue from funds	41.8%	65.3%	74.9%
67	All other income	58.2%	34.7%	25.1%
	LIQUIDITY			
68	Total loans & leases - net/Total lcy deposits*	40.6%	27.3%	17.2%
69	Liquid assets/Total lcy deposits**	64.6%	87.2%	97.7%
70	Demand deposits/Total lcy deposits	12.0%	9.4%	8.4%
71	Savings deposits/Total lcy deposits			
72	Time deposits/Total lcy deposits	68.2%	81.9%	78.3%
73	Inter-bank borrowings/Total lcy deposits	19.8%	8.7%	13.3%
74	Interest expense - banks/Interest expense	74.9%	57.2%	38.8%
75	**NET FOREIGN CURRENCY ASSETS (LIABILITIES)**	7,065,056	(48,562)	(4,952,292)

**Net loans not funded by free capital as a % of local currency deposits*
*** Liquid assets adjusted for inter-bank takings*

CORONATION MERCHANT BANK LIMITED

	KEY RATIOS CONT'D	31-Dec-2019	31-Dec-2018	31-Dec-2017
	ASSET QUALITY			
76	Performing loans (N'000)	72,742,231	54,340,867	32,247,778
77	Non-performing loans (N'000)			
78	Non-performing loans/Total loans - Gross			
79	Loan loss provision/Total loans - Gross	0.1%	0.1%	0.0%
80	Loan loss provision/Non-performing loans			
81	Risk-weighted assets/Total assets & contingents	56.8%	50.5%	40.7%
	CAPITAL ADEQUACY			
82	Adjusted capital/risk weighted assets (Basel II)	14.0%	12.7%	21.5%
83	Tier 1 capital/Adjusted capital	97%	132%	129%
84	Total loans - net/Adjusted capital	0.39	0.30	0.44
85	Capital unimpaired by losses (N'000)	27,920,968	26,694,645	23,523,045
	STAFF INFORMATION			
86	Net earnings per staff (N'000)	85,732	84,643	119,610
87	Staff cost per employee (N'000)	11,611	11,464	12,138
88	Staff costs/Operating expenses	26.3%	26.6%	19.7%
89	Average number of employees	121	125	85
90	Average staff per branch	40	42	28
	OTHER KEY INFORMATION			
91	Legal lending limit(N'000)	13,960,484	13,347,323	11,761,523
92	Number of branches	3	3	3
93	Age (in years)	4	3	2
94	Government stake in equity (Indirect)	Nil	Nil	Nil
		Estimates	**Actual**	**Actual**
	MARKET SHARE OF INDUSTRY TOTAL	2019	2018	2017
95	Lcy deposits (excluding interbank takings)	0.54%	0.79%	0.50%
96	Total assets & contingents	0.80%	0.67%	0.46%
97	Total loans & leases - net	0.46%	0.43%	0.24%
98	Net earnings	0.38%	0.46%	0.48%
99	Profit before tax	0.54%	0.67%	0.69%
100	Cash dividend	1.62%	0.55%	0.36%

RATING DEFINITIONS

Aaa	A financial institution of impeccable financial condition and overwhelming capacity to meet obligations as and when they fall due. Adverse changes in the environment (macro-economic, political and regulatory) are unlikely to lead to deterioration in financial condition or an impairment of the ability to meet its obligations as and when they fall due. In our opinion, regulatory and/or shareholder support will be obtained, if required.
Aa	A financial institution of very good financial condition and strong capacity to meet its obligations as and when they fall due. Adverse changes in the environment (macro-economic, political and regulatory) will result in a slight increase the risk attributable to an exposure to this financial institution. However, financial condition and ability to meet obligations as and when they fall due should remain strong. Although regulatory support is not assured, shareholder support will be obtained, if required.
A	A financial institution of good financial condition and strong capacity to meet its obligations. Adverse changes in the environment (macro-economic, political and regulatory) will result in a medium increase in the risk attributable to an exposure to this financial institution. However, financial condition and ability to meet obligations as and when they fall due should remain largely unchanged. In our opinion, shareholder support should be obtainable, if required.
Bbb	A financial institution of satisfactory financial condition and adequate capacity to meet its obligations as and when they fall due. It may have one major weakness which, if addressed, should not impair its ability to meet obligations as and when due. Adverse changes in the environment (macro-economic, political and regulatory) will result in a medium increase in the risk attributable to an exposure to this financial institution.
Bb	Financial condition is satisfactory and ability to meet obligations as and when they fall due exists. May have one or more major weaknesses. Adverse changes in the environment (macro-economic, political and regulatory) will increase risk significantly.
B	Financial condition is weak but obligations are still being met as and when they fall due. Has more than one major weakness and may require external support, which, in our opinion, is not assured. Adverse changes in the environment (macro-economic, political and regulatory) will increase risk significantly.
C	Financial condition is very weak. Net worth is likely to be negative and obligations may already be in default.
D	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.

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