

Access Bank BRS

Global Rating Scale: B+/Stable/B

Nigerian Rating Scale: NgA-

Strengths

- Currently Good Levels of Capitalisation, threatened by high risk asset growth
- Beyond Adequate Profitability, given the high risk
- Focus on high end Corporate Nigeria

Weaknesses

- High Credit Risk caused by rapid Growth, Some High Concentrations
- Relatively Strained Funding & Liquidity in a Nigerian Banking Context
- High Economic and Industry Risk associated to operating in Nigeria

Rationale

The ratings on Access are constrained by the bank's rapid business expansion and high credit and operational risks in the Federal Republic of Nigeria (foreign currency BB-/Stable/B; local currency BB/Stable/B). Another key negative rating factor is the bank's strained funding and liquidity profile. The ratings are supported by the bank's good capitalization, adequate profitability and a focus on top-tier domestic corporates. The ratings on Access reflect the bank's stand-alone credit profile and do not factor in extraordinary support.

Access Bank is a corporate-focused institution operating in the middle tier of the Nigerian banking sector. While the credit risk of the loan portfolio benefits from the bank's focus on creditworthy customers, rapid loan growth in an untested environment, high loan concentrations, and exposure to foreign currency loans and margin lending, exacerbate these risks. On a positive note, Access operates with a good level of capitalization and reserves, which gives some comfort to increasing credit risks. The ratings also benefit somewhat from relatively embedded risk management tools and processes, as well as quite strong senior management compared with some of its domestic peers. Nevertheless, continuation of rapid loan growth could weaken capitalization and further strain the bank's funding and liquidity profile. The bank's loan-to-deposit ratio of 126% on Dec. 31, 2008 is already high and its liquid asset cushion is relatively small. Profitability is adequate, but good returns are moderated by the high risk profile and strong inflation in Nigeria. High economic and industry risks--including low wealth and education levels, weak judiciary, poor corporate governance, and infrastructural deficiencies--exacerbate the credit and operational risks inherent to banks operating in Nigeria.

Outlook

The stable outlook balances the deteriorating domestic operating environment and the bank's good capitalization and adequate profitability. Negative ratings action would follow a significant deterioration in asset quality, capitalization, or liquidity profile. Continuous aggressive expansion would also be viewed as a negative rating factor as it is a threat to long-term creditworthiness because it exacerbates credit and operational risks.

Lower credit and operational risks, alongside improvements to the funding and liquidity profile of the bank could result in a positive rating

Profile – A Corporate Focused Institution Experiencing Too High Growth

With total assets of NGN800 Billion (USD\$5.6 Billion at USD1 to NGN141) at Dec. 31, 2008 Access Bank PLC is a middle tier financial institution operating in the competitive Nigerian banking sector. Access was founded 1989 but was bought out by the existing management in 2002. Further transformation occurred in 2005 when Senior Management entered the mass banking sector consolidation process with two goals, to retain both the overall control of the enlarged entity and the corporate focus of the institution. Consequently, Access approached two smaller foreign owned institutions which benefitted from relatively stronger systems and corporate relationships. Post consolidation an aggressive period of integration ensued and all operations transferred within a 3month period. This process was made easier as management did not attempt to actively merge cultures or transfer senior management from the merger partners. During the boom of the Nigerian Banking Sector that followed the consolidation process, Access experienced three years of continually very high growth, which exacerbate the already high credit and operational risks associated to operating in the Nigerian Banking Sector. Gross loans increased by over 100% per annum for each of the past three years, including 105% annualised growth in the first 9 months leading to Dec. 31, 2008. As well as high balance sheet growth the bank was also challenged to rapidly expand its staff and network. At Sept. 30, 2008 the banks network included 230 ATM's, 131 branches and an electronic banking platform.

Access view themselves as primarily a high end corporate focused financial institution, although in reality the bank is equally exposed to Nigeria's emerging commercial sector. This is in part due to the 'value chain' banking strategy, which is common to Nigerian financial services but it is also the economic sector of greatest opportunity. At Dec. 31, 2008 Access had 150 high end corporate customers, defined as well structured companies with over NGN3Billion turnover that provided 40% of revenues, 40% of deposits and 54% of loans. At the same date the bank had 6,500 commercial customers including the public sector and companies with over NGN 100 million turnover, which provided 40% of revenues, 32% of deposits and 40% of loans. 50% of commercial customers are not value chain clients. The public sector provides less than 6% of liabilities and 3% of assets. 400,000 retail cliental, provide only 3% of revenues, 8% of deposits and 3% of loans and are currently kept for the strategic intent of supporting corporate banking services. Business diversification is therefore considered to be weak, as revenues are dependent on Nigeria's narrow corporate sector. Access Bank has followed its multinational customer base into eight Central, East & West of Africa countries and the United Kingdom. Despite having full banking licenses the international subsidiaries operate effectively as branches and, due to their limited size and relatively youth, currently offer no revenue diversification. Whilst management do not rule out M&A activity domestic combinations and large external acquisitions are unlikely in the short term. International subsidiaries are expected to provide no more than 10% of revenues going forward.

Support and Ownership- a neutral ratings factor

The ratings on Access reflect the standalone creditworthiness of the institution and do not include any uplift of extraordinary external support. We do not consider Access to be a systemically important institution. However even for such banks, due to our classification of Nigeria as supportive, we do not add notches of support due to government support. Standard & Poor's considers that although the government may act to save the first tier banks in the case of an individual bank crisis, its ability to provide timely financial support in a time of economic stress is not assured.

Access Bank is a public owned company listed on the Nigerian Stock Exchange (NSE). Over the past 6 months the share price of Access Bank has dropped by 60% from its peak value, making it one of the largest fallers on the turbulent NSE. This fall reflected the flight of foreign investors and the margin lending bubble burst, rather than the fundamentals of the bank. At Jan. 13, 2009 the bank's market capitalisation was USD\$400 million. Ownership is well diversified, comprising over 450,000 individual shareholders although the largest shareholders are the Mr Aig-Imoukhuede (CEO) and Mr Wigwe (Deputy CEO) who indirectly owned over 5% in the bank. In total the 14 man board of directors own 21.13% of the bank.

Strategy- Remain corporate focused but increase Banking Services

Access Bank aims to rank among the top 5 banking groups in Nigeria. Positively management expect its very high growth to decline in 2009, with strategic emphasis changing from maximising growth to producing more sustainable levels of growth. Management expect around 35% organic growth in 2009 and 30% in 2010. Therefore although the bank is likely to remain in the second tier of Nigerian banks by asset size the reduction in growth is viewed positively by Standard & Poor's as it will somewhat lower currently high credit and operational risks. Given the high risk asset growth and straining liquidity, deposit mobilisation is likely to be a key regard for Access bank in 2009. However, competition for the targeted non interest bearing deposits is fierce and wealth levels have dropped in Nigeria since the oil price highs in early 2008.

The high end corporate focus is set to remain, as management view its skills and understanding in this sector to be its main competitive advantage. Consequently, Access have been developing their investment banking capabilities, and are currently considered to be one of the larger capital and debt market advisories. To compete with other large banking groups and offer a complete suite of financial service products, the bank added an asset management subsidiary, a mortgage subsidiary and a share registrar in 2008. Insurance has been overlooked as the risk management is complex. Access entrance in to the retail banking market was somewhat later than Nigerian Peers and currently it makes a limited balance sheet impact. However, the bank has been increasing its products and channels in order to target High Net Worth Individuals (HNWI) and employees of its corporate cliental. The balance sheet impact of Commercial banking sector is expected to grow, especially in regards to liabilities and revenues, as the expensive roll out of branch network will start to become profitable. Positively the bank actively minimises its exposure to the public sector.

Risk Profile and Management- Dominated By Rapid Growth

The risk profile of Access is dominated by its high credit and operational risks inherent to operating in Nigeria, but exacerbated by high growth levels. Rapid expansion of branch networks, risks assets and product ranges whilst embedding risk management processes is considered a strain on managerial and operational capabilities. Leverage is high for a Nigerian bank, and currently adequate asset quality figures are flattered by high loan growth. Credit risks are also raised by high loan concentrations, reflecting the high end corporate focus of the bank. Access bank's liquidity is also weaker than top tier rated peers, although it still remains adequate by international standards. Mobilising funds is set to be a key challenge for the bank in 2009.

Enterprise Risk Management; Weak

Enterprise risk management (ERM) at the bank is considered to be weak. This opinion balances relatively embedded internal controls and processes with an aggressive, albeit recently moderated, risk appetite. Operating in Nigeria exposes the bank to above average operational risks, including security, legal, fraud and political risks. Operational risk management has been active for just over one year, staff appear to be aware of risks, but online reporting platforms are still being built.

High Credit Risks Resulting from Rapid Growth and Large Loan Concentrations

Credit risks are dominated by high credit growth and large loan concentrations in an untested debt culture with poor corporate governance, narrow economic base. From Mar. 31, 2008 to Dec. 31, 2008 loans grew by 105% on an annualised basis. In the opinion of Standard & Poor's any institutions ability to manage credit risk is strained by such aggressive credit growth. Rapid growth has also increased leverage to high levels, in comparison to Nigerian peers, with gross loans accounting for 60% of total assets. Positively the bank slowed lending growth down significantly in the last quarter of 2008. Furthermore the loan book remains very short term, with 85% of loans maturing within one year, which gives the bank strong flexibility to respond to any problems or just to increase liquidity. Credit risk somewhat benefits from the banks focus on the top tier of corporate Nigeria. Although commercial lending is a rapidly growing part of the portfolio, corporate lending with 150 clients still accounts for 54% of total loans. Retail lending accounted for only 3% of total lending. Consequently single name concentrations are high, with the top twenty on and off balance sheet exposures accounting for approximately 44% of gross loans and 112% of Adjusted Total Equity (ATE). Positively exposures are relatively well collateralised, although creditor rights are yet to be truly tested in an economic downturn. The loan portfolio is also somewhat concentrated by industry, with the Oil & gas sector contributing 33% of total loans, manufacturing at 11%, and Financial services 10%. Margin lending represented about 8% of total lending in November 2008, although this is a significant reduction since its peak. Margin lending activities were stopped in mid 2008, and our expectations are that most will work off the balance sheet in the medium term with a small number of non performing loans resulting from them. However, the bank will still be exposed to the turbulent NSE by the large amount of share collateral, which accounts for 15% of total collateral. Credit quality is also exposed to the rapidly depreciating Naira, with 30% of loans denominated in foreign currency (mostly in USD). Positively all foreign currency lending is afforded only to corporate borrowers whose turnover is denominated in that foreign currency.

Asset quality indicators are currently adequate, although they currently underestimate credit risks as they benefit somewhat from rapid loan growth and remain untested through a full economic cycle. Nonperforming loans accounted for 3.5% of gross lending at Dec. 31, 2008, which in percentage terms is stable from March but in nominal terms has shown large growth. Restructured loans accounted for a further 2% of total loans. NPL ratios also benefitted from strong write offs, with over NGN 5 billion in 2007. Loan loss provisioning levels are adequate, covering expected losses with reserves covering 117% of non performing loans and 4% of gross loans at Dec. 31, 2008. Standard & Poor's encourage the maintenance of provisions due to the high USD and margin lending exposure.

Market Risk at Access is limited.

The bank partakes in the proprietary trading of T-Bills, bonds and a small amount of basic FX. Positively there are no ambitions to trade equities, commodities or exotic currencies. Interest rate risks are well monitored and somewhat mitigated by the short term nature of the balance sheet. Most lending is extended with a fixed rate but with a covenant meaning the bank can reprice quickly. Foreign currency risk occurs in the small open position between USD lending and deposits, although this has been limited to 1% of shareholder funds by the Central Bank of Nigeria.

Funding and Liquidity- A Ratings Weakness

The funding profile of Access Bank benefits from some diversification but it is restrained by a reliance on less stable overseas correspondent bank lines, albeit that they are largely matched by currency and tenor to the loan book. At Sept. 30, 2008 deposits accounted for 68% of total funds, mainly deriving from the corporate and commercial sector. The strong corporate focus is seen as a slight source of competitive disadvantage, as it somewhat excludes the bank from the large and stable non interest bearing deposit market available from the retail and public sectors. Access has made use of international lines for customer Letters of Credit and on lending facilities, such funds represented 26% of balance sheet funds at Sept. 30, 2008 and are matched by currency and tenor in the loan book. Other funding sources include interbank funds (c5% of total funds) and a 3 year domestic NGN12 billion bond (c5% of total funds), which expires Dec. 31, 2009. Consequently, although the loan to deposit ratio of 146% at Sept. 30, 2008 is very high in comparison to rated peers this is mitigated by the matched on lending facilities. Nevertheless the liquidity profile of Access is considered to be weaker than tier one rated peers. At Dec. 31, 2008 liquid cash, money market instruments and securities accounted for 33% of total balance sheet assets. This liquid asset cushion is low in comparison to rated Nigerian peers and in part reflects a conscious decision to maximise the efficiency of the balance sheet. Liquidity somewhat benefits from the short term nature of lending operations, with 44% of loans maturing within 3 months. Although **% of deposits mature within 3 months, the majority is considered core and stable. For ratings to improve Standard & Poor's would need to see a track record of improved liquidity management.

Adequate Profitability Reflecting Good Returns but High Growth and Tight Liquidity

With return on adjusted assets of 3% in the first nine months of its 2009 financial year, the profitability of Access Bank is considered to be moderate in a Nigerian Banking Sector context. In 2009 lower business growth including restrained lending volumes

could restrain interest revenues and associated fees; however recurring fees and commissions and high interest rates should keep revenues high. Furthermore cost control is good and the provisioning is relatively robust therefore the bank can afford to be relatively flexible on the expenditure side to maintain the bottom line.

Reflecting the focus on corporate Nigeria revenues suffer from a lack diversification. Corporate, commercial and investment banking (mainly treasury, trading and some asset management) contributed 46%, 40% and 14% of revenues in the 2008 financial year. Currently geographic diversification is limited; to date the consolidated West African subsidiaries remain loss making. Even within Nigerian most business is concentrated in Lagos, Port Harcourt and Abuja reflecting the business and public sector centres of the country. Interest income is the primary driver of revenues. At Sept. 30, 2008 68% of total revenues were derived from interest income and of that 59% came from loans, 3% interbank placements and 38% securities. Margins are strong, reflecting the high loan growth and leveraging of the balance sheet and the aggressive targeting of low cost funds. Recurring Fees and Commissions provided a solid 32% of revenues in the first half of the 2009 financial year. Commission on deposit account turnover and lending facilities fees are the largest contributors of such income. Profitability is not reliant on volatile market sensitive incomes. Cost control is a strong focus for the bank and consequently the efficiency of Access compares well to rated peers, with a noninterest expenses to revenues ratio of 47% in the first six months of 2009. Cost of risk is also currently quite low but this is likely to increase in the medium term as credit volumes slow and the loan portfolio quality deteriorates due to the economic slowdown, foreign currency and margin lending exposures.

The accounts are consolidated and prepared by KPMG according to Nigerian Accounting Standards, the framework for which is characterised as weak. Access year end is March, 31, 2008.

Good Levels of Capitalisation, potentially threatened by high growth and aggressive dividends

With a capital adequacy ratio of 28% and a Standard & Poor's adjusted total equity to adjusted assets ratio of 23.4% at Dec. 31, 2008 the capitalisation of Access Bank is considered to be currently good. The capital cushion provides enough room to allow for restrained medium term growth however capital levels could quickly come under pressure if the rapid growth of loans continues and aggressive dividends restrain internal capital creation. Standard & Poor's views the defence of adequate capital ratios as an important ratings driver in the Nigerian banking sector. Financial flexibility has been severely reduced since the significant falls on the Nigerian Stock exchange. Investors are not likely to be as supportive to any financial institution raising equity in Nigeria as they were in 2006, 2007 and early 2008. Access Bank aims to maintain a Capital Adequacy Ratio of 20%, which should be an adequate capital cushion even in a Nigerian Banking sector context.