Outlook On South African Banks Now Negative After Same Action On Sovereign; National Scale Ratings Lowered

November 26, 2019

PRIMARY CREDIT ANALYST

Samira Mensah
Johannesburg
(27) 11-214-4869
samira.mensah@spglobal.com

SECONDARY CONTACTS

Trevor Barsdorf
Johannesburg
+ 27 11 214 4852
trevor.barsdorf@spglobal.com

Sahil Tribhowan
Johannesburg
(27) 11-214-4862
sahil.tribhowan@spglobal.com

Motlanalo Mashoene
Johannesburg
motlanalo.mashoene@spglobal.com

Overview

- On Nov. 22, 2019, S&P Global Ratings revised its outlook on South Africa to negative on weakening fiscal and debt trajectory and sizable contingent liabilities.
- We do not rate financial institutions in South Africa above the foreign currency sovereign ratings, due to the direct and indirect impacts a sovereign distress would have on banks' operations.
- We have therefore revised the outlook to negative from stable on FirstRand Bank Ltd., FirstRand Ltd., Nedbank Ltd., Investec Bank Ltd., Capitec Bank Ltd., and African Bank Ltd. We affirmed our global scale ratings on all of these entities.
- At the same time, we have lowered our long-term national scale ratings on Absa Bank Ltd., FirstRand Bank Ltd., FirstRand Ltd., Nedbank Ltd., Investec Bank Ltd., and BNP Paribas Personal Finance South Africa Ltd, and we have affirmed our short-term national scale ratings on these entities.
- In addition, we have affirmed our global and national scale ratings on African Bank Ltd. and Capitec Bank Ltd.

JOHANNESBURG (S&P Global Ratings) Nov. 26, 2019--S&P Global Ratings Services today revised its outlook to negative from stable on FirstRand Bank Ltd., FirstRand Ltd., Nedbank Ltd., Investec Bank Ltd., Capitec Bank Ltd., and African Bank Ltd. We affirmed our 'BB/B' long- and short-term global scale issuer credit ratings on FirstRand Bank Ltd., Nedbank Ltd., Investec Bank Ltd., and Capitec Bank Ltd. We also affirmed our 'B+/B' issuer credit ratings on FirstRand Ltd. and African Bank Ltd.

At the same time, we lowered to 'zaAA' from 'zaAA+' our South African long-term national scale ratings on FirstRand Bank Ltd., Nedbank Ltd., Absa Bank Ltd., Investec Bank Ltd., and BNP Paribas Personal Finance South Africa Ltd., and affirmed the short-term national scale ratings at 'zaA-1+'. We also lowered our long- and short-term national scale ratings on FirstRand Ltd. to 'zaA-/zaA-2' from 'zaA/zaA-1'. In addition, we affirmed our 'zaAA/zaA-1+' national scale ratings on Capitec Bank Ltd. and our 'zaA-/zaA-2' national scale ratings on African Bank Ltd.

Finally, as a result of this review, we lowered our national scale ratings on the debt issued by the aforementioned entities (see ratings list), including lowering to 'zaAA' from 'zaAA+' our national scale rating on the South African rand (ZAR) 10 billion DMTN program issued by BNP Paribas (South Africa Branch).

Rationale

The rating actions follow the outlook revision on the foreign currency rating on South Africa on Nov. 22, 2019 (see "South Africa Outlook Revised To Negative On Worsening Fiscal And Debt Trajectory; Ratings Affirmed," published on RatingsDirect). We do not rate financial institutions in South Africa above the foreign currency sovereign ratings, due to the direct and indirect impacts that a sovereign distress would have on banks' operations. That said, we acknowledge that, amid challenging macro and industry changes, South Africa's banking performance has been fairly resilient. We expect sector-wide pressure on revenues but broadly, stable earnings as banks continue to streamline costs.

The sovereign outlook revision to negative points to the constraints related to very low GDP growth and high fiscal deficits, which is causing an increasingly unsustainable debt trajectory. Disappointing economic performance has stemmed from weak investor sentiment and low investment, power shortages, dry weather, and limited reform momentum. We now expect growth for this year will slow to 0.6%, down from our expectation of 1.0% in May 2019, then average 1.8% through 2022. Unemployment has worsened to 29.1%, a 16-year high. The poor macroeconomic performance has materially deteriorated the fiscal outlook and hit tax revenue generation. South Africa now faces the two-pronged challenge of reinstating fiscal credibility while simultaneously restoring inclusive economic growth.

The South African economy could suffer a sharp increase in credit risk and a contraction of the banking sector. The lack of progress on policy reforms and an enfeebled economic environment could further weaken households' resilience, given their already-high levels of debt. Total private sector credit (defined as total household debt, corporate debt from the banks, and capital markets) will remain steady at 85% of GDP on average through 2021, on the back of a weak economy but stable inflation. Private sector investments are unlikely to be significant as long as domestic constraints, including inadequate electricity supply and an overall weak business confidence, persist. That said, we believe that small pockets of lending exist in the renewable energy space, as well as in personal loans and mortgages in the mid- market.

In contrast with other emerging markets, there is no sign of economic imbalances stemming from asset price bubbles in South Africa. The domestic housing market has recorded flat growth in real terms over the past four years, supported by historically moderate interest rates and slow increases in housing supply. Commercial real estate continues to exhibit lower credit losses than we would normally expect in a muted environment, partly because leverage is low for such exposures while vacancy rates are rising. In addition, domestic household leverage remains a significant source of risk for the sector because of South Africa's lower wealth levels than in other emerging markets. The risk of capital outflows will linger for the funding of the current account deficit, which we forecast will stabilize at 3.9% of GDP. Portfolio flows can be susceptible to changes in foreign investor sentiment because of the high share of sovereign debt holdings and an increase in U.S. interest rates.

We see negative trends in economic risks. Our view is based on potentially higher credit losses due to persistently low economic growth alongside the high leverage of domestic households, which are vulnerable to inflation and interest rates. Economic risks could also increase, in our opinion, if household debt leverage metrics deteriorate to levels seen in 2010-2012. This would lower further our overall view of the sector's resilience to economic shocks and could lead us to revise down our anchor for South African banks. We project credit losses will normalize at 1.2% in 2020 for top South African banks. There is a pronounced difference between top-tier banks' and second-tier banks' credit losses. Although the latter's are a fraction of the size of the large banks', they dominate credit losses. Positively, provisioning levels appear to have improved since 2017, partly due to the change in the nonperforming loan mix toward unsecured from secured lending, and the new impairment charges rules from International Financial Reporting Standards 9.

Meanwhile, the South African banking sector continues to derive funding predominately from short-term wholesale deposits. In addition, the sector is exposed to concentrations from nonbank financial institutions since retail savings are low and contractual savings tend to be managed by professional money managers. Still, we believe that local currency liquidity will remain intact because of the South African Reserve Bank's (SARB's) foreign exchange oversight of South African residents and companies. Most importantly, the banking sector is not overly exposed to external funding, and remains in a net creditor position.

We expect the SARB's committed liquidity facility to fall away by year-end 2022 because banks have fully complied with the liquidity coverage ratio ahead of schedule. An additional pack of reforms will likely be introduced gradually to meet Basel IV requirements. Furthermore, we continue to believe that a deposit insurance scheme, and ultimately an effective resolution regime, will be implemented over the next 12-18 months.

Until we have more clarity on the resolution regime's implementation, we do not apply extraordinary support in the form of additional loss-absorbing capacity to issuer credit ratings on South African banks.

Outlook

The outlook on FirstRand Bank Ltd., FirstRand Ltd., Nedbank Ltd., Investec Bank Ltd., and Capitec Bank Ltd. are negative and reflect the outlook on South Africa.

We could lower the ratings on these banks if we were to lower our sovereign ratings. This is because we do not rate financial institutions in South Africa above the foreign currency sovereign ratings, due to the direct and indirect impacts a sovereign distress would have on banks' operations.

We could revise the outlook to stable if we took the same action on South Africa. This could occur if we saw a substantial improvement in the economic growth outlook. Outside a sovereign action, we see positive or negative rating actions on these banks as a remote possibility in the next 12 months.

Our negative outlook on African Bank Ltd. indicates rising risks in the economy. We would lower the ratings on African Bank Ltd. if increasing economic imbalances result in higher credit losses or if rule of law is challenged, further amplifying credit risks. We would also lower the ratings if our risk-adjusted capital decreases below 15% or if the bank's liquidity buffers deteriorated materially due to higher than expected loan growth. We would revise the outlook to stable if, all else equal, we foresaw a stabilization of risks in the economy.

We do not assign outlooks to national scale ratings. However, our national scale ratings on Absa Bank Ltd. and BNP Personal Finance South Africa Ltd. would likely move in line with any rating action on South Africa.

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- Criteria | Financial Institutions | General: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Financial Institutions | Banks: Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises, Dec. 19, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Criteria | Financial Institutions | Banks: Assessing Bank Branch Creditworthiness, Oct. 14, 2013
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria | Financial Institutions | Banks: Commercial Paper I: Banks, March 23, 2004

Related Research

- South Africa Outlook Revised To Negative On Worsening Fiscal And Debt Trajectory; Ratings Affirmed, Nov. 22, 2019
- Banking Industry Country Risk Assessment: South Africa, Sept. 5, 2019

Ratings List

***************** Absa Bank Ltd. *****************		
Downgraded; Ratings Affirmed		
	To	**From**
Absa Bank Ltd.		
South Africa National Scale	zaAA/--/zaA-1+	zaAA+/--/zaA-1+
**************** African Bank Ltd. ****************		
Outlook Action; Ratings Affirmed		
	To	From
African Bank Ltd.		
Issuer Credit Rating	B+/Negative/B	B+/Stable/B
South Africa National Scale	zaA-/--/zaA-2	zaA-/--/zaA-2
Senior Unsecured	B+	B+
****************** BNP Paribas *****************		
Downgraded; Ratings Affirmed		
	To	**From**
BNP Paribas Personal Finance South Africa Ltd.		
South Africa National Scale	zaAA/--/zaA-1+	zaAA+/--/zaA-1+
**************** Capitec Bank Ltd. ****************		
Outlook Action; Ratings Affirmed		
Capitec Bank Ltd.		
Issuer Credit Rating	BB/Negative/B	BB/Stable/B
South Africa National Scale	zaAA/--/zaA-1+	zaAA/--/zaA-1+
***************** FirstRand Ltd. *****************		
Outlook Action; Ratings Affirmed; Downgraded		
	To	**From**
FirstRand Ltd.		
Issuer Credit Rating	B+/Negative/B	B+/Stable/B
South Africa National Scale	zaA-/--/zaA-2	zaA/--/zaA-1
FirstRand Bank Ltd.		
Issuer Credit Rating	BB/Negative/B	BB/Stable/B
South Africa National Scale	zaAA/--/zaA-1+	zaAA+/--/zaA-1+
Senior Unsecured	BB	BB
Subordinated	B+	B+
Subordinated	zaA+	zaAA-
Junior Subordinated	zaA-	zaA

*** * * * * * * * * * * * * * Investec Bank Ltd. * * * * * * * * * * * * * ***		
Outlook Action; Ratings Affirmed; Downgraded		
	To	**From**
Investec Bank Ltd.		
Issuer Credit Rating	BB/Negative/B	BB/Stable/B
South Africa National Scale	zaAA/--/zaA-1+	zaAA+/--/zaA-1+
*** * * * * * * * * * * * * * Nedbank Group Ltd. * * * * * * * * * * * * * ***		
Outlook Action; Downgraded; Ratings Affirmed		
	To	**From**
Nedbank Ltd.		
Issuer Credit Rating	BB/Negative/B	BB/Stable/B
South Africa National Scale	zaAA/--/zaA-1+	zaAA+/--/zaA-1+

Regulatory Disclosures

- Primary credit analyst: Samira Mensah, Director (Nedbank Ltd.)
- Primary credit analyst: Trevor Barsdorf, Associate Director (FirstRand Bank Ltd., FirstRand Ltd., Investec Bank Ltd., Capitec Bank Ltd., BNP Paribas Personal Finance South Africa Ltd.)
- Primary credit analyst: Sahil Tribhowan, Associate Director (Absa Bank Ltd., African Bank Ltd.)
- Chairperson: Nigel Greenwood

Date initial rating assigned:

- Absa Bank Ltd.: Nov. 30, 2015
- African Bank Ltd.: April 5, 2016
- BNP Paribas Personal Finance South Africa Ltd.: Nov. 15, 2016
- Capitec Bank Ltd.: Oct. 13, 2015
- FirstRand Bank Ltd.: Oct. 29, 1999
- FirstRand Ltd.: April 14, 2011
- Investec Bank Ltd.: Feb. 19, 2014
- Nedbank Ltd.: Dec. 10, 2012

Date of previous review:

- Absa Bank Ltd.: July 2, 2018
- African Bank Ltd.: April 30, 2019
- BNP Paribas Personal Finance South Africa Ltd.: April 5, 2019
- Capitec Bank Ltd.: Sept. 13, 2018
- FirstRand Bank Ltd.: July 2, 2018

- FirstRand Ltd.: July 2, 2018
- Investec Bank Ltd.: July 2, 2018
- Nedbank Ltd.: July 2, 2018

Disclaimers

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

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

Materials Used In The Credit Rating Process: Sufficient information in general consists of both (i) financial statements that describe the Issuer's financial condition, results of operations and cash-flows, and (ii) a description of the activities and obligations of the entity including of its governance and legal structure.

This credit rating was disclosed to the rated entity or related third party before being issued.

S&P Global Ratings' regulatory disclosures (PCRs) are published as of a point-in-time, which is current as of the date a Credit Rating Action was last published. S&P Global Ratings updates the PCR for a given Credit Rating to include any changes to PCR disclosures only when a subsequent Credit Rating Action is published. Thus, disclosure information in this PCR may not reflect changes to data within PCR disclosures that can occur over time subsequent to the publication of a PCR but that are not otherwise associated with a Credit Rating Action.

Glossary

- Counterparty credit rating: A form of issuer credit rating, which is a forward-looking opinion about an obligor's overall creditworthiness.
- Credit losses: Loan loss provisions to average customer loans expressed as a percentage.
- Date initial rating assigned: The date S&P Global Ratings assigned the long-term foreign currency issuer credit rating on the entity.
- Date of previous review: The date S&P Global Ratings last reviewed the credit rating on the entity.
- Funding and liquidity: A combined assessment of the strength and stability of a bank's funding mix and its ability to manage its liquidity needs in adverse market and economic conditions over an extended period.
- Group credit profile (GCP): S&P Global Ratings' opinion of a group's creditworthiness as if the group were a single legal entity, and is conceptually equivalent to an ICR. A GCP does not address any specific obligation.
- National scale rating: An opinion of an obligor's creditworthiness or overall capacity to meet

specific financial obligations, relative to other issuers and issues in a given country or region.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.