MOODY'S
INVESTORS SERVICE

Rating Action: Moody's assigns first-time local currency deposit ratings of Ba1 to First National Bank of Namibia Limited. Outlook Negative.

13 Dec 2019

London, 13 December 2019 -- Moody's Investors Service has today assigned to First National Bank of Namibia Limited (FNB Namibia) Ba1/Not Prime long-term and short-term local currency deposit ratings and Ba3/Not Prime long-term and short-term foreign currency deposit ratings. The outlook on the Ba1 local currency deposit rating is negative, in line with the issuer rating of South Africa, where FNB Namibia's ultimate parent and support provider, FirstRand Limited (unrated), resides. Conversely, the outlook on the Ba3 foreign currency deposit rating is stable, in line with the stable outlook on the issuer rating of Namibia. Moody's also assigned Counterparty Risk Assessments (CR Assessment) of Baa3(cr)/P-3(cr) and Counterparty Risk Ratings (CRR) of Baa3/P-3 to FNB Namibia.

A full list of the bank's ratings is at the end of this press release.

The local currency deposit rating of Ba1 assigned to FNB Namibia incorporates two notches of rating uplift from the bank's Baseline Credit Assessment (BCA) of ba3 on account of our very high expectation of support from its ultimate parent, South Africa's FirstRand Limited (unrated), in a stress scenario. As a result, the local currency deposit rating of Ba1 is one notch higher than Namibia's sovereign issuer rating of Ba2.

FNB Namibia's Ba3 long-term foreign currency deposit rating is constrained by Namibia's long-term foreign currency deposit ceiling.

RATINGS RATIONALE

BASELINE CREDIT ASSESSMENT

FNB Namibia's BCA, its standalone credit strength, of ba3 captures the bank's: (1) strong domestic franchise, which will support its earnings generating capacity and robust capital ratios, providing a large buffer against loan losses; and (2) material investment in improving its risk management capabilities in recent years. These strengths are moderated by FNB Namibia's: (1) deterioration in asset quality metrics on account of the weak operating environment in Namibia, which is further compounded by the bank's high exposure to mortgages; and (2) high reliance on short-term institutional deposit funding, a structural issue for all large Namibian banks; though we note that historically these deposits have been sticky.

STRONG DOMESTIC FRANCHISE SUPPORTS EARNINGS GENERATING CAPACITY AND ROBUST CAPITAL RATIOS, PROVIDING A LARGE BUFFER AGAINST LOAN LOSSES

FNB Namibia's BCA is underpinned by its strong franchise in Namibia, being the country's largest bank (28% market share in total assets), which supports both its robust capital buffers and earnings by attracting cheap deposits and good quality borrowers. As of June 2019, Moody's adjusted tangible common equity (TCE) as a percentage of risk-weighted assets (RWA) stood at 14.5%. FNB Namibia's Moody's adjusted TCE to RWA ratio is markedly higher than the global ba3 BCA peer median of 12.4%, as of October 2019. We expect the bank's capitalisation to remain resilient, primarily because of FNB Namibia's strong profitability metrics, with a net income to tangible assets ratio of 2.4%, as of June 2019, versus the ba3 BCA median of 1.1%. Going forward, on account of the weak growth environment that will translate into higher provisioning costs and lower loan growth, we expect downward pressure on FNB Namibia's earnings. However, the bank's recent investments in digitization will partially offset weaker profitability by supporting non-interest revenue and reducing operating expenses (operating expenses fell 6% year-on-year, as of June 2019, and management attributes this decline to its digitization efforts). Effective management of operating costs to date has meant that the bank's cost-to-income ratio is relatively low at 52%, as of June 2019, versus 58% for the Namibian banking system.

DETERIORATION IN ASSET QUALITY METRICS IS COMPOUNDED BY THE BANK'S HIGH EXPOSURE TO MORTGAGES BUT PARTIALLY MITIGATED BY IMPROVEMENTS TO RISK MANAGEMENT CAPABILITIES

More negatively, FNB Namibia's standalone credit profile also reflects its deteriorating nonperforming loan (NPL) metrics. Moody's adjusted NPLs increased moderately to 2.71%, as of June-end 2019, from 1.66%, as June-end 2018 (the industry average was 4.4%, or 5.2% excluding FNB Namibia, as of June 2019). This deterioration in NPLs is on account of the sluggish macro environment in Namibia which has negatively impacted the repayment capacity of borrowers. Additionally, the ongoing drought in Namibia is reflected in the disproportionally high contribution to total NPLs of 10% from the agriculture sector (4.4% of FNB Namibia's loans are to the agriculture sector).

We view FNB Namibia's high exposure to mortgages as another source of asset risk for the bank. As of June 2019, FNB Namibia's mortgage and commercial property loan portfolio was 56% of total loans (banking system average was 52%, as of December 2018). House prices contracted 11% over the first 6 months of 2019 and, as a result, have reduced the equity borrowers hold in their properties. However, falling homeowner equity is mitigated by: (1) the significant portion of FNB Namibia's mortgage book that is first-lien mortgages, and thus holds first priority interest on the property asset; (2) the principal repayment terms of all mortgages (FNB Namibia does not offer interest only mortgages); and (3) the significant housing deficit in Namibia that supports property prices (in a 2018 report, the government estimates the housing backlog at 100,000 units increasing at a yearly rate of 3,700).

Additionally, over the last 3 years, FNB Namibia has built up its risk management team and has been ramping up investments in its Namibia-based risk management infrastructure. As such, we expect any further deterioration in FNB Namibia's NPLs to be manageable.

HIGH RELIANCE ON SHORT-TERM INSTITUTIONAL DEPOSIT FUNDING AND RELATIVELY MODEST LIQUIDITY

FNB Namibia's BCA also reflects the bank's high reliance on short-term institutional deposit funding, a structural issue for all major Namibian banks. As of June 2019, customer deposits made up about 67% of the bank's liabilities. However, only 32% of deposits are retail (includes small and medium-sized enterprises), the rest coming from non-bank financial depositors (31%), corporates (29%) and government (8%). Contractually, 67% of deposits are due within 3 months whereas 76% of loans mature after 1 year (the standard term of an FNB Namibia mortgage is 20 years). This asset-liquidity mismatch leaves FNB Namibia with a large negative net liquidity gap. However, we expect deposits from non-bank financial institutions, corporates and government to be stable over the next 12 to 18 months reflecting their historical behaviour. FNB Namibia's Liquid Banking Assets to Tangible Banking Assets ratio has gradually increased over time to 26%, as of June 2019, from 20%, as of June 2016, but remains lower than comparable international peers.

RATINGS OUTLOOK

The negative outlook on FNB Namibia's local currency deposit ratings reflects the negative outlook on the issuer rating of South Africa, where FNB Namibia's ultimate parent and support provider, FirstRand Limited (unrated), resides.

The stable outlook on FNB Namibia's foreign currency deposit ratings reflects the stable outlook on Namibia's sovereign issuer rating given that the bank's foreign currency deposit ratings are constrained by Namibia's foreign currency deposit ceiling of Ba3. This ceiling reflects transfer and convertibility risks associated with foreign currency deposits in the event of a government default. Additionally, the stable outlook reflects Moody's view that FNB Namibia's asset risks and profitability metrics will stay within the thresholds assumed by its current ratings despite the deteriorating trend witnessed over the last 18 months.

Moody's does not have any particular environmental, social and governance concerns for FNB Namibia and did not apply any corporate behavior adjustment. Nonetheless, corporate governance remains a key credit consideration and requires ongoing monitoring.

STRUCTURAL CONSIDERATIONS

AFFILIATE SUPPORT

FNB Namibia's ratings incorporate our very high expectation of support by its ultimate parent, FirstRand Limited, based on FirstRand Limited's 58% indirect ownership of the bank and FNB Namibia's association with FirstRand Limited's brand (including the use of its logos).

GOVERNMENT SUPPORT CONSIDERATIONS

FNB Namibia's ratings do not benefit from any government support uplift given that its adjusted BCA of ba1 is above Namibia's sovereign issuer rating of Ba2. Notwithstanding, we assume a 'High' probability of government support in case of need given the bank's systemic importance (FNB Namibia is Namibia's largest bank with a 28% market share in terms of total assets).

FACTORS THAT COULD LEAD TO AN UPGRADE

Given the negative outlook, an upgrade of the bank's local currency deposit ratings is unlikely at this stage. However, a stabilization of the outlook could be triggered by a stabilization of the issuer outlook of South Africa, where the ultimate parent and support provider, FirstRand Limited, resides.

FNB Namibia's foreign currency deposit ratings could be upgraded in the event of an upgrade of Namibia's sovereign issuer ratings and ceilings.

FACTORS THAT COULD LEAD TO A DOWNGRADE

FNB Namibia's local currency deposit ratings could be downgraded if the credit profile of FirstRand Limited deteriorated or if we assess that FirstRand Limited's willingness to provide support in future will decline below our current assumptions. FNB Namibia's foreign currency deposit ratings could be downgraded if Namibia's issuer rating and ceilings are downgraded. Lastly, any significant deterioration in the financial profile of FNB Namibia could negatively impact the bank's standalone credit profile and deposit ratings.

LIST OF AFFECTED RATINGS

..Issuer: First National Bank of Namibia Limited

Assignments:

.... Adjusted Baseline Credit Assessment, Assigned ba1

.... Baseline Credit Assessment, Assigned ba3

.... Long-term Counterparty Risk Assessment, Assigned Baa3(cr)

.... Short-term Counterparty Risk Assessment, Assigned P-3(cr)

.... Long-term Counterparty Risk Ratings, Assigned Baa3

.... Short-term Counterparty Risk Ratings, Assigned P-3

.... Long-term Bank Deposit Rating (Foreign Currency), Assigned Ba3 Stable

.... Long-term Bank Deposit Rating (Local Currency), Assigned Ba1 Negative

.... Short-term Bank Deposit Ratings, Assigned NP

Outlook Action:

Outlook Assigned Negative(m)

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Banks Methodology published in November 2019. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

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