FitchRatings

31 Mar 2020 | Downgrade

# Fitch Downgrades South African Banks to 'BB', Negative Outlook on Coronavirus Impact

Fitch Ratings-London-31 March 2020:

Fitch Ratings has downgraded the Long-Term Issuer Default Ratings (IDRs) and Viability Ratings (VRs) of five South African banks - Absa Bank Limited, FirstRand Bank Limited, Investec Bank Limited, Nedbank Limited and The Standard Bank of South Africa Limited - to 'BB' and 'bb', respectively. The Outlook on all the IDRs is Negative.

Fitch has taken similar rating actions on the Long-Term IDRs and VRs of four South African bank holding companies, namely Absa Group Limited, Investec Limited, Nedbank Group Limited and Standard Bank Group Limited. All National Long-Term Ratings and debt ratings (where applicable) have also been downgraded. The Outlook on the National Long-Term Ratings is revised to Negative from Stable.

The rating action is driven by the expected negative impact from the coronavirus outbreak on the banks' operating environment and key financial metrics, notwithstanding uncertainty as to the full economic and financial market implications.

We believe the South African operating environment is particularly exposed to the pandemic because of its highly dense and vulnerable communities, and heightened macro-economic risk from falling commodity prices, disruption to tourism, mining activity and manufacturing, as well as pressure on the country's public finances.

The 21-day 'lockdown' that started on March 27 will deliver a further large negative shock to the banks' operating environment, which was already affected by the country's very weak economic outlook. Downside risks could extend beyond this, given the risk of a prolongation of the crisis and South Africa's reliance on global export markets.

Fitch expects South African banks to face multiple challenges in the near team, including a decline in client activity, lower interest rates, which will put pressure on margins, and rising credit losses. These factors will increase risks to banks' earnings, asset quality and capitalisation. Debt-relief measures announced by banks will not only affect margins but also mask the extent of asset-quality deterioration.

The South African Reserve Bank (SARB) recently cut the repo rate by 100bp to 5.25% and announced a range of additional liquidity support measures, including government bond purchases in the secondary market, to increase market liquidity. Further measures from the SARB, including the relaxation of bank rules to ensure the flow of credit into the economy, are likely.

Fitch had already anticipated a more challenging year for banks in 2020 - as reflected in its Negative 2020 sector outlook - mainly due to weak GDP growth. Our expectations of earnings and asset-quality weakening for 2020 now far exceed what was contemplated in late 2019 when we published our outlook.

The first-order effects on banks' asset quality will mainly come from households and businesses with more exposure to industries and asset classes affected by the coronavirus, and these stressed loans may not be visible before banks' 2020 first-half results are published. The second-order effects will come from both households and SMEs due to the weaker growth outlook, and will largely depend on the duration and severity of the crisis. We expect prime corporates to have adequate buffers to absorb shocks, at least into 2021.

Debt Securities Under Criteria Observation

Following the application of Fitch's updated Bank Rating Criteria, the agency has increased the notching for Tier 2 issues of Standard Bank Group, Absa Group, FirstRand Bank and Investec Bank to two notches from one from the respective VR and National Rating anchor ratings. Conditions that would justify an alternative notching under our criteria are not met, in our view.

Fitch has also widened the notching between the IDR and the long-term debt rating assigned to Standard Bank Group's USD4 billion debt programme to one from zero to reflect (under the new criteria) below-average recovery prospects because of thin Qualifying Junior Debt buffers. For the same reason, we have widened the notching to one from zero between Absa Group's National Long-Term Rating and the National Rating on Absa Group's ZAR50 billion DMTN programme. Conditions that would justify an alternative notching under our criteria are not met, in our view.

All affected ratings have been removed from Under Criteria Observation, where they were placed on 5 March 2020.

Absa Group Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)

; Viability Rating; Downgrade; bb
----subordinated; Long Term Rating; Downgrade; B+
----senior unsecured; National Long Term Rating; Downgrade; A+(zaf)
----subordinated; National Long Term Rating; Downgrade; A(zaf)
----senior unsecured; National Short Term Rating; Affirmed; F1+(zaf)
Nedbank Group Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)
; Viability Rating; Downgrade; bb
Standard Bank Group Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)
; Viability Rating; Downgrade; bb
----senior unsecured; Long Term Rating; Downgrade; BB-
----subordinated; Long Term Rating; Downgrade; B+
----senior unsecured; Short Term Rating; Affirmed; B
The Standard Bank of South Africa Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)
; Viability Rating; Downgrade; bb
----senior unsecured; Long Term Rating; Downgrade; BB
----senior unsecured; Short Term Rating; Affirmed; B
Absa Bank Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)
; Viability Rating; Downgrade; bb
----senior unsecured; Long Term Rating; Downgrade; BB
----senior unsecured; Short Term Rating; Affirmed; B
----senior unsecured; National Long Term Rating; Downgrade; AA-(zaf)

Investec Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)
; Viability Rating; Downgrade; bb
Investec Bank Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)
; Viability Rating; Downgrade; bb
----senior unsecured; Long Term Rating; Downgrade; BB
----senior unsecured; Short Term Rating; Affirmed; B
----subordinated; National Long Term Rating; Downgrade; A(zaf)
FirstRand Bank Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)
; Viability Rating; Downgrade; bb
----senior unsecured; Long Term Rating; Downgrade; BB
----subordinated; Long Term Rating; Downgrade; B+
----senior unsecured; Short Term Rating; Affirmed; B
----senior unsecured; National Long Term Rating; Downgrade; AA-(zaf)
----subordinated; National Long Term Rating; Downgrade; A(zaf)
----senior unsecured; National Short Term Rating; Affirmed; F1+(zaf)
Nedbank Limited; Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; Short Term Issuer Default Rating; Affirmed; B
; Local Currency Long Term Issuer Default Rating; Downgrade; BB; RO:Neg
; National Long Term Rating; Downgrade; AA-(zaf); RO:Neg
; National Short Term Rating; Affirmed; F1+(zaf)
; Viability Rating; Downgrade; bb
----senior unsecured; Long Term Rating; Downgrade; BB
----senior unsecured; Short Term Rating; Affirmed; B

Key Rating Drivers

IDRs and VRs

The Long-Term IDRs of all South African banks are driven by their standalone creditworthiness, as defined by their VRs.

The banks benefit from sound franchises and enjoy strong market shares (the so-called big four, each with sector assets of about 20%, and Investec with 8%), as well as highly diversified business profiles that underpin a certain stability of earnings and solid risk-management frameworks. The banks also have solid funding and liquidity profiles, underpinned by large customer deposit funding bases and limited external funding reliance. However, with operations largely concentrated in the riskier South African operating environment, banks are exposed to heightened downside risks to asset quality, earnings and capital metrics.

Fitch analyses South African banking groups based on a consolidated assessment of the group. Ratings assigned to bank holding companies are equalised with the consolidated risk assessment of the groups given low double leverage at the holding company level, as well as high capital and liquidity fungibility within the group.

NATIONAL RATINGS

The National Ratings reflect the issuers' creditworthiness relative to other South African issuers.

RATING SENSITIVITIES

IDRs, VRs and NATIONAL RATINGS

The Long-Term IDRs, VRs and National Ratings of all issuers are sensitive to deterioration in asset quality, profitability and capital in the challenging operating environment. Downside risks are heightened by the coronavirus outbreak especially if there is a more severe economic and financial market fallout. The VRs are also sensitive to a multi-notch downgrade of South Africa's sovereign rating.

Ratings could be upgraded if there was a significant improvement in operating conditions, with no material impact on banks' financial profiles from the stress. However, no South African bank meets Fitch's criteria to be rated above the sovereign. There is currently no upside potential to ratings.

The National Ratings are also sensitive to a change in the banks' creditworthiness relative to other South African issuers.

The banks' debt ratings are sensitive to any change in their respective IDRs, VRs and National

Ratings, where applicable.

Best/Worst Case Rating Scenario

Ratings of financial institutions have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon, and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING
The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations
ESG issues are credit neutral or have only a minimal credit impact on the entity(ies), either due to their nature or the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

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Additional information is available on www.fitchratings.com

The following issuer(s) did not participate in the rating process, or provide additional information, beyond the issuer's available public disclosure: FirstRand Bank Limited

**Applicable Criteria**

Bank Rating Criteria (pub. 28 Feb 2020) (including rating assumption sensitivity)
National Scale Ratings Criteria (pub. 18 Jul 2018)
Short-Term Ratings Criteria (pub. 06 Mar 2020)

**Additional Disclosures**

Dodd-Frank Rating Information Disclosure Form
Solicitation Status

With respect to this RAC, if the lead analyst is based in an EU-registered entity, the issuer(s) will be displayed below in the following colour when the ratings provided are unsolicited and the issuer(s) did not participate in the rating process, or provide additional information beyond the issuer's available public disclosure.

**Non-Participating Unsolicited Issuers**

**FirstRand Bank Limited**
**FirstRand Bank Limited USD 500 mln 4.25% Notes 30 Apr 2020**
**FirstRand Bank Limited ZAR 829 mln 5.5% Notes 7 Dec 2023**
**FirstRand Bank Limited ZAR 130 mln 10.75% Notes 10 Dec 2024**

**FirstRand Bank Limited ZAR 200 mln 9.5% Notes 21 Feb 2031**
**FirstRand Bank Limited ZAR 250 mln 8% Notes 14 Apr 2045**
**FirstRand Bank Limited USD 1.5 bln EMTN Programme - Senior**
**FirstRand Bank Limited ZAR 30 bln  Domestic MTN programme - Senior**
**FirstRand Bank Limited ZAR 80 bln Domestic MTN Programme**
**FirstRand Bank Limited ZAR 2 bln Subordinated Tier II Notes**
**FirstRand Bank Limited ZAR 2 bln Tier 2 Floating Rate Subordinated Notes 6 Mar 2025**
**FirstRand Bank Limited ZAR 1.75 bln Floating Rate Subordinated Tier II Notes 8 Jul 2025**
**FirstRand Bank Limited ZAR 148 mln Floating Rate Subordinated Notes 2 Jun 2026**
**FirstRand Bank Limited ZAR 125 mln Floating Rate Subordinated Notes 2 Jun 2026**
**FirstRand Bank Limited ZAR 601 mln Floating Rate Subordinated Tier II Notes 8 Jan 2027**

Endorsement Status
Endorsement Policy

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