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Ratings

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Capitec Bank Ltd.

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Capitec Bank Ltd.

SACP	bb	+	Support	0	+	Additional Factors	-1

Anchor	bb+	
Business Position	Moderate	-1
Capital and Earnings	Strong	+1
Risk Position	Moderate	-1
Funding	Average	0
Liquidity	Strong	

ALAC Support	0
GRE Support	0
Group Support	0
Sovereign Support	0

Issuer Credit Rating
BB-/Stable/B

Credit Highlights

Overview	
Key strengths	**Key risks**
Strong capitalization and significant capital buffers.	Higher credit losses than peers, given targeted segment focus.
Large balance-sheet liquidity that compares better with domestic peers.	Focus on unsecured lending, although diversification is increasing.
Robust operational and credit-risk management framework, and conservative provisioning policy.	

Capitec Bank Ltd.'s (Capitec's) profitability should start recovering in fiscal 2022 (ended Feb. 28, 2022), however, asset quality metrics will remain relatively constrained. S&P Global Ratings forecasts the bank's profitability will start increasing after a sharp decline in 2021, supported by lower provisions and moderate loan growth. We forecast the group's return on equity (ROE) will increase to above 25% from 16% in 2021. Although economic activity has started picking up, we expect nonperforming loans (NPLs) and cost of risk to marginally decrease but remain high at 5.0%-6.5% and 4.5-6.5% by year-end fiscal 2022 from 9.4% and 10.5% in 2021, respectively. This is because credit risk remains high, particularly for low-income households.

The bank continues to increase product and earnings diversification through client selection, product offerings, and noninterest income. The group has seen increasing product diversification, balancing its mix of lending and transactional income by moving into higher-income segments, and away from unsecured retail lending. This has been further supported by the widening of product offerings and target markets via a new business banking division (following the Mercantile Bank Ltd. acquisition).

Capitec's strong capital and earnings continue to support the rating. We believe Capitec's strong capital and earnings support its standalone assessment, while its risk position reflects comparatively higher credit losses. We expect the risk-adjusted capital (RAC) ratio to remain a credit strength and forecast it will stay higher than 12% through fiscal 2024. We expect Capitec to continue to display considerably higher credit losses than its top South African banking peers, which is a relative credit weakness.

Outlook: Stable

The stable outlook on Capitec Bank mirrors the outlook on South Africa.

Downside scenario

We believe downgrade prospects are limited within the next year and would most likely arise following further deterioration of the sovereign credit rating. This could happen if economic prospects fail to recover during the forecast period, and financing pressures increase.

Upside scenario

We believe an upgrade is unlikely for Capitec in the next year, partly because any improvement in the bank's stand-alone credit profile (SACP), by itself, would not result in an upgrade if our sovereign credit rating is unchanged. Over the medium term, an improvement in South Africa's credit quality would likely result in a higher rating for the bank.

Key Metrics

Capitec Bank Ltd.--Key Ratios And Forecasts

	--Fiscal year ended Feb. 28--				
(%)	**2018a**	**2019a**	**2020a**	**2021f**	**2022f**
Growth in operating revenue	6.9	11.2	8.8	11.8-14.4	9.5-11.6
Growth in customer loans	15.2	38.1	(1.0)	6.8-8.3	7.2-8.8
Net interest income/average earning assets (NIM)	11.2	9.3	7.6	7.8-8.7	8.1-8.9
Cost to income ratio	38.4	39.6	40.0	39.0-41.0	39.5-41.5
Return on average common equity	26.2	26.5	16.1	22.8-25.2	23.6-26.1
New loan loss provisions/average customer loans	8.7	6.8	10.5	6.1-6.7	5.1-5.6
Gross nonperforming assets/customer loans	6.1	6.4	9.4	5.9-6.5	4.9-5.4
Risk-adjusted capital ratio	12.6	12.7	11.8	12.2-12.8	12.9-13.6

All figures are S&P Global Ratings-adjusted. a--Actual. f--Forecast. NIM--Net interest margin.

Anchor:'bb+' For Banks Concentrated In South Africa

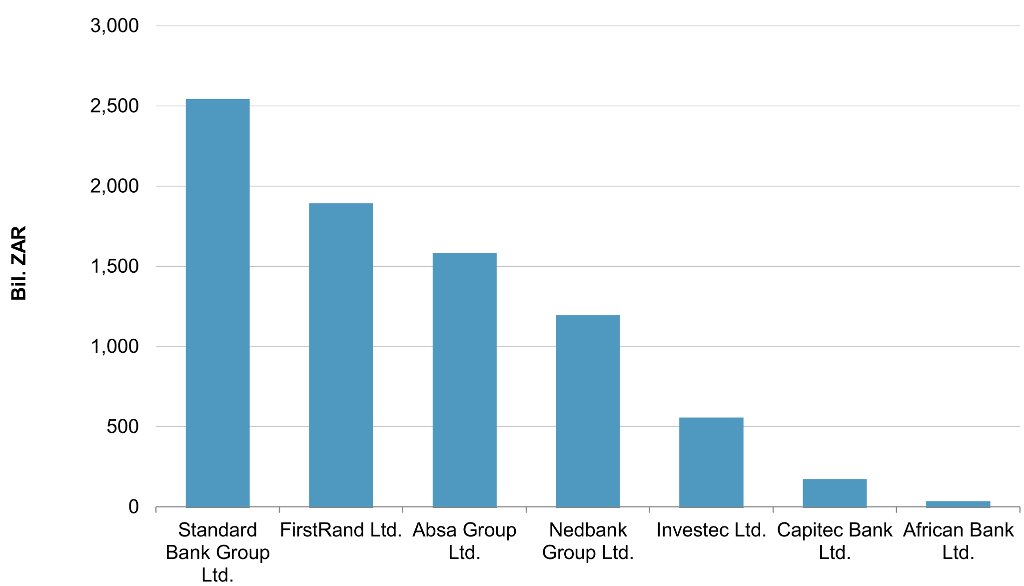
We use our Banking Industry and Country Risk Assessment (BICRA) economic and industry risk scores to determine a bank's anchor, the starting point in assigning an issuer credit rating. The anchor for a commercial bank operating only in South Africa is 'bb+', reflecting our economic risk score of '7' and industry risk score of '5'.

Business Position: A Mid-Tier Bank With A Widening Focus

Capitec is a retail-focused bank operating in South Africa's stable banking sector, with total assets of South African rand (ZAR) 167 billion (approximately $11 billion) as of Aug. 31, 2021. Retail banking in South Africa is highly competitive. Capitec positions itself as the leading retail franchise in the country through the delivery of a low-cost alternative to traditional banks. It provides simple savings and loan products with transparent and affordable pricing and convenient customer-centric services. The bank continues to diversify its income streams through different product offerings (such as funeral cover, home and car loans, and small and midsize enterprise [SME] offerings), as well evolving underlying unsecured offerings. Although we note the increased diversification, we still believe that Capitec's historical focus can expose it to earnings volatility in times of stress. However, the diversification efforts will add scale and support the bank's competitive position while strengthening its revenue stability and earnings diversification.

Chart 1

South African Banks Total Assets (*YTD 2021)
Total asset size relative to other players

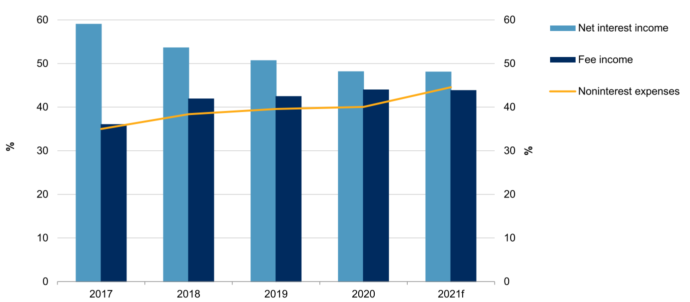


YTD--Year till date. *Capitec as at Aug. 31, 2021; Standard Bank Group Ltd., FirstRand Ltd, Absa Group, and Nedbank Group as at June 30, 2201; African Bank Ltd. and Investec Ltd. as at March 31, 2021. ZAR--South African rand. Source: Company financials.

Revenue stability has been supported by increased noninterest income through accelerated digitalization of the bank and its customer base. Capitec's operating performance was affected by COVID-19, like the rest of the domestic banking sector, although operating metrics improved markedly in fiscal 2021, augmented by the sale of funeral and credit life insurance products. The bank also has the benefit of operating efficiency, with its cost-to-income ratio trending below 40%. Historically, Capitec has posted a robust return on average common equity of 26%. However, this decreased to 16% in fiscal 2021 due to higher provisions amid high market uncertainty in calendar 2020. Profitability has since improved to 25% as of first-half 2021, amid lower net credit provisions. In our opinion, we expect profitability to move back above 25% over the forecast period.

Chart 2

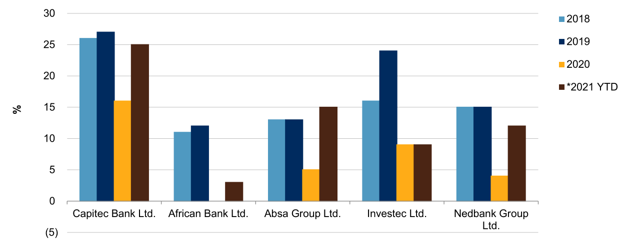
Interest Income Versus Noninterest Income, And Noninterest Expense (Relative To Operating Revenue)
Fee income supports revenue amid a sustained shift toward digital revenue



f--Forecast. Source: S&P Global Ratings.

Chart 3

Capitec Has Posted Favorable Earnings Compared To Peers Through The Cycle
Return on equity remains above that of peers



YTD--Year to date. *Capitec as at Aug. 31, 2021, Nedbank Group and Absa Group as at June 30, 2021, and African Bank Ltd. and Investec Ltd as at March 31, 2021. Source: S&P Global Ratings.

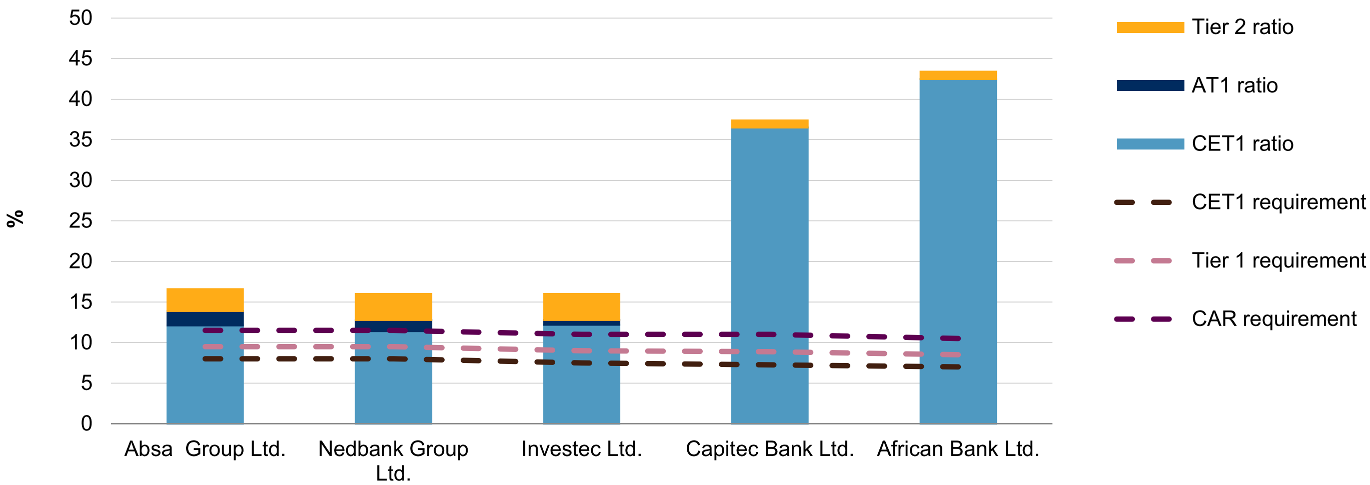
Capital And Earnings: Strong Capital Despite Earnings Volatility

We expect Capitec to maintain its strong capital position despite earnings volatility. We calculate our RAC ratio for Capitec at 11.8% as of Feb. 28, 2021, which is well above that of most South African banks. We expect our RAC ratio will remain above 12% over the next 12-18 months. Our forecast takes in account the following assumptions:

- Loan growth of about 7.5% in fiscal 2022, before rising to 8%-10% in subsequent periods. Although we see that loan growth was negative for fiscal 2021 because of COVID-19-related lockdowns, we expect it will pick up in fiscal 2022 as economic activity has started to recover. Moreover, the business the Mercantile Bank acquisition will provide new business avenues for the group.
- Net interest margin to remain slightly compressed in fiscal 2022, reflecting the low interest rate environment.
- Operating efficiency to remain broadly stable at about 40% over next two years, supported by effective cost management by the group.
- Cost of risk to moderate at 5.0%-6.5% in fiscal 2022-2023 after increasing to about 11% in fiscal 2021 because of conservative provisioning amid the COVID-19 pandemic.

Chart 4

Capitec's Regulatory Capital Is Comfortably Above The Regulatory Minimum And Compares Well With Domestic Peers'



CET1--Common equity Tier 1. AT1--Additional Tier 1. CAR--Capital adequacy ratio. Capitec as at Aug. 31, 2021 2021, African Bank Ltd., Absa Group and Nedbank Group as at June 30, 2021, Investec Ltd Group as at March 31, 2021. Source: Banks' pillar III reports.

Risk Position: Inherently High Risk Costs And Still Concentrated Risk Exposure

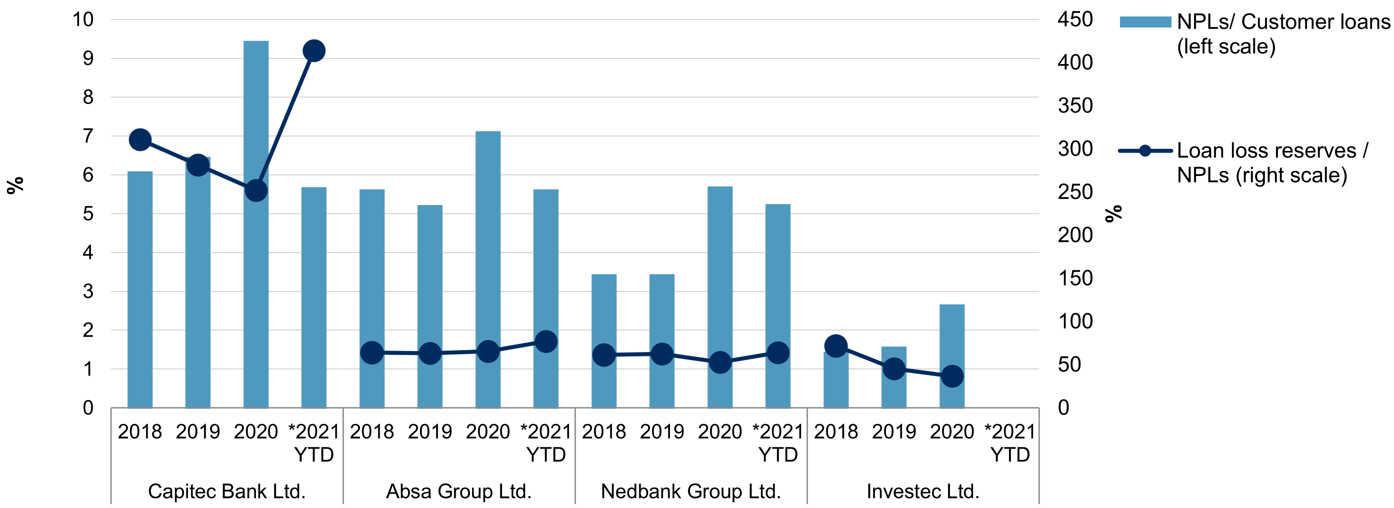
Our assessment of Capitec's risk position incorporates the bank's comparatively higher credit losses, which we do not fully capture in our RAC calculation. The bank's loan losses are considerably higher than those of South African top-tier banks, which operate with more diversified, lower-risk profiles, and lower-margin loan products. We also factor in the still concentrated nature of the loan book. The acquisition of Mercantile Bank will support wider product offerings and increased diversification, specifically within the SME space.

Gross loans dropped 1% during fiscal 2021. This was in line with the bank's reduced risk appetite amid rising credit risk within the economy, both before and during the pandemic. The bank has deliberately sought to enhance its risk profile through tighter credit policies and risk selection. This has been accompanied by an increase in average loan size, with tenors exceeding five years accounting for about 19% of the loan book for the six months ended Aug. 31, 2021, compared with 9% on Feb. 28, 2016.

As of Feb. 28, 2021, net charge-offs increased to 10.4% of average customer loans from 6.9% on Feb. 28, 2020. We anticipate net charge-offs to average customer loans will gradually decline and remain at 5.5%-6.5%, while credit losses (new loan-loss provisions to average customer loans) will start declining in fiscal 2022 and then improve further in fiscal 2024, at 6.5%-7.0%.

Chart 5

Capitec's Asset Quality Metrics Are Still Elevated Relative To South African Peers' Given Its Target Market Segment



YTD--Year to date. NPLs--Nonperforming loans. *Capitec as at Aug. 31, 2021, Nedbank Group and Absa Group as at June 30, 2021, and Investec Ltd. as at March 31, 2021. Source: S&P Global Ratings.

Funding And Liquidity: Retail Deposit Funded But Cost Of Funds Is Higher Than Peers'

The bank is funded mainly through retail deposits accounting for 87% of total funding as of Feb. 28, 2021. This supports strong liquidity coverage ratios relative to those of other South African banks. Capitec's stable funding ratio improved to 168% for fiscal 2021 (fiscal 2020: 155%). As of May. 31, 2021, the bank's liquidity coverage ratio of 2,908% as of first-half 2021 (compared with fiscal 2021's 2,486%) far exceeded the sector average because of the high level of retail customer deposits. This is further seen with broad liquid assets to short-term wholesale funding at 118% at fiscal 2021 (from 2020's 92%).

Support: No External Support

We consider government support for the banking sector uncertain, owing to the anticipated resolution regime and the regulator's demonstrated appetite for senior creditor bail-in.

Additional Rating Factors: Sovereign Foreign Currency Ratings Are Below The SACP

Although we assess Capitec's SACP at 'bb', the long-term rating on the bank is limited by our foreign currency rating on the sovereign. We do not rate South African banks above the sovereign because of the likely direct and indirect impact of sovereign stress on banks.

Environmental, Social, And Governance

We consider Capitec's core business focus to have a limited environmental impact since its lending is not susceptible to transition risk. We recognize the bank's focus on financial literacy and inclusion through increasing product awareness among the population. Capitec's governance framework is not an outlier compared with peers' and the bank operates with similar standards to the wider South African financial sector.

Key Statistics

Table 1

Capitec Bank Ltd.--Key Figures

	--Year ended Feb. 28--				
(Mil. ZAR)	***2022**	**2021**	**2020**	**2019**	**2018**
Adjusted assets	163,759.0	154,016.0	132,951.6	99,875.0	84,674.2
Customer loans (gross)	77,681.0	75,026.0	75,783.3	54,879.0	47,642.5
Adjusted common equity	30,483.0	28,378.0	24,118.3	19,690.0	17,416.4
Operating revenues	12,826.0	22,998.0	21,142.8	19,020.9	17,798.6
Noninterest expenses	5,716.0	9,210.0	8,370.4	7,297.4	6,223.5
Core earnings	3,916.0	4,704.0	6,475.4	5,483.0	4,598.6

*As at Aug. 31, 2021. ZAR--South African rand.

Table 2

Capitec Bank Ltd.--Business Position

	--Year ended Feb. 28--				
(%)	***2022**	**2021**	**2020**	**2019**	**2018**
Total revenues from business line (Mil. ZAR)	12,826.0	22,998.0	21,142.0	19,021.0	17,798.6
Return on average common equity (%)	25.4	16.1	26.5	26.2	25.7

*As at Aug. 31, 2021. ZAR--South African rand.

Table 3

Capitec Bank Ltd.--Capital And Earnings

	--Year ended Feb. 28--				
(%)	***2022**	**2021**	**2020**	**2019**	**2018**
Tier 1 capital ratio	36.5	35.9	29.6	34.0	34.1
S&P RAC ratio before diversification	N/A	11.8	12.7	12.6	13.9
S&P RAC ratio after diversification	N/A	10.1	11.0	10.8	11.8
Double leverage	N.M.	97.0	96.2	96.3	99.8

Table 3

Capitec Bank Ltd.--Capital And Earnings (cont.)

	--Year ended Feb. 28--				
(%)	*2022	2021	2020	2019	2018
Net interest income/operating revenues	48.1	48.1	50.6	53.7	59.1
Fee income/operating revenues	43.8	43.9	42.4	41.9	36.0
Noninterest expenses/operating revenues	44.6	40.1	39.6	38.4	35.0
Preprovision operating income/average assets	8.8	9.5	10.9	12.7	14.6
Core earnings/average managed assets	4.9	3.2	5.5	5.9	8.8

*As at Aug. 31, 2021. N/A--Not Applicable. N.M--Not Meaningful. RAC--Risk-adjusted capital.

Table 4

Capitec Bank Ltd.--Risk-Adjusted Capital Framework Data

(Mil. ZAR)	Exposure*	Basel III RWA	Average Basel III RW(%)	S&P Global Ratings' RWA	Average S&P Global Ratings' RW (%)
Credit risk					
Government and central banks	40,446.0	0.0	0.0	37,161.0	92.0
Of which regional governments and local authorities	0.0	0.0	0.0	0.0	0.0
Institutions and CCPs	44,310.0	17,142.0	39.0	55,272.0	125.0
Corporate	4,937.0	4,241.0	86.0	7,719.0	156.0
Retail	56,751.0	59,411.0	105.0	80,646.0	142.0
Of which mortgage	3,075.0	3,075.0	100.0	2,301.0	75.0
Securitization§	0.0	0.0	0.0	0.0	0.0
Other assets†	7,144.0	10,719.0	150.0	18,701.0	262.0
Total credit risk	153,587.0	91,513.0	60.0	199,499.0	130.0
Credit valuation adjustment					
Total credit valuation adjustment	--	11.0	--	0.0	--
Market risk					
Equity in the banking book	0.0	0.0	0.0	0.0	0.0
Trading book market risk	--	446.0	--	670.0	--
Total market risk	--	446.0	--	670.0	--
Operational risk					
Total operational risk	--	33,195.0	--	41,493.0	--
	Exposure	**Basel III RWA**	**Average Basel II RW (%)**	**S&P Global Ratings' RWA**	**% of S&P Global Ratings' RWA**
Diversification adjustments					
RWA before diversification	--	125,166.0	--	241,662.0	100.0
Total diversification/ concentration adjustments	--	--	--	38,903.0	16.0
RWA after diversification	--	125,166.0	--	280,565.0	116.0

Table 4

Capitec Bank Ltd.--Risk-Adjusted Capital Framework Data (cont.)

	Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global Ratings' RAC ratio (%)
Capital ratio				
Capital ratio before adjustments	27,899.0	22.3	28,404.0	11.8
Capital ratio after adjustments‡	27,899.0	22.3	28,404.0	10.1

*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions. ‡Adjustments to tier 1 ratio are additional regulatory requirements (e.g. transitional floor or pillar 2 add-ons). RWA--Risk-weighted assets. RW--Risk weight. RAC--Risk-adjusted capital. ZAR--South Africa Rand. Sources: Company data as of Feb. 28, 2021, S&P Global Ratings.

Table 5

Capitec Bank Ltd.--Risk Position

	--Year ended Feb. 28--				
(%)	***2022**	**2021**	**2020**	**2019**	**2018**
Growth in customer loans	7.1	(1.0)	38.1	15.2	5.6
Total managed assets/adjusted common equity (x)	5.5	5.5	5.6	5.1	4.9
New loan loss provisions/average customer loans	5.4	10.5	6.9	8.7	11.4
Net charge-offs/average customer loans	6.5	10.4	6.9	8.7	11.6
Gross nonperforming assets/customer loans + other real estate owned	5.7	9.4	6.4	6.1	8.3
Loan loss reserves/gross nonperforming assets	414.1	252.2	281.4	311.1	146.5

*As at 31 August 2021.

Table 6

Capitec Bank Ltd.--Funding And Liquidity

	--Year ended Feb. 28--				
(%)	***2022**	**2021**	**2020**	**2019**	**2018**
Core deposits/funding base	98.1	96.0	93.9	93.4	90.3
Customer loans (net)/customer deposits	46.1	48.3	62.3	62.4	72.3
Long term funding ratio	99.8	99.1	99.3	99.5	98.8
Stable funding ratio	149.8	167.8	154.9	155.9	174.3
Net broad liquid assets/short-term customer deposits	49.6	62.2	57.4	62.7	79.4

*As at Aug. 31, 2021.

Related Criteria

- 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: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 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: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- South Africa Banking Sector Recovery Will Be Gradual Due To Lingering Effects Of The Pandemic, June 01, 2021
- South Africa Ratings Affirmed At 'BB-/B' Foreign Currency And 'BB/B' Local Currency; Outlook Stable, May 21, 2021

Regulatory Disclosures

Regulatory disclosures applicable to the most recent national and global scale credit rating action can be found at "Various Rating Actions Taken On South African Banks Following Sovereign Downgrade ," published May 7, 2020, on Ratings Direct.

Glossary

- ALAC: Additional Loss-Absorbing Capacity, which can provide extraordinary external support for banks.
- Anchor: The starting point for assigning a bank a long-term rating, based on economic and industry risk.
- Asset-liability mismatch: Occurs when financial terms of an institution's assets and liabilities do not correspond.
- Asset quality: A key measure of the quality and performance of the assets of a bank.
- Available stable funding: Core deposits, plus deposits due to banks (net of those that mature within one year), plus other borrowings (net of maturities within one year), plus total equity, minus intangibles.
- Broad liquid assets: cash (net of restricted cash) and reserves at central bank, plus other cash and money market, plus bank loans and reverse repos that mature in less than one year, plus total liquid assets.
- Business position: A measure of the strength of a bank's business operations.
- Capital and earnings: A measure of a bank's ability to absorb losses.
- Counterparty credit rating: A form of issuer credit rating, which is a forward-looking opinion about an obligor's overall creditworthiness.
- Credit losses: Losses arising from credit risk.
- Credit risk: Risk that a borrower will default on its payment obligations.
- Customer loans (gross): Total customer loans before loan loss reserves.

- 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.
- Funding base: Total deposits, plus acceptances, repurchase agreements, and other borrowings (including commercial papers, short- and long-term debt, subordinated debt, and minimal equity content hybrids).
- Gross nonperforming assets over customer loans plus other real estate owned over customer loans: Nonaccrual loans, plus restructured loans, plus repossessed assets plus loans 90-days past due; over gross customer loans plus repossessed assets.
- Group support: An assessment of the likelihood that a parent or other group member would provide extraordinary support to a bank within that group.
- Loan loss reserves over gross nonperforming assets: General plus specific reserves, over adjusted nonperforming assets (nonaccrual loans plus restructured loans plus repossessed assets plus 90-day past due loans).
- Long term funding ratio: Available stable funding, over funding base plus total equity, minus intangibles.
- 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.
- New loan loss provisions over average customer loans: Credit loss provisions (including specific loan provisions and general and other provisions) minus recoveries, over average gross customer loans of current period and last fiscal year.

Anchor Matrix

Industry Risk	**Economic Risk**									
	1	2	3	4	5	6	**7**	8	9	10
1	a	a	a-	bbb+	bbb+	bbb	-	-	-	-
2	a	a-	a-	bbb+	bbb	bbb	bbb-	-	-	-
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+	-	-
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	-
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	**bb+**	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7	-	bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+
8	-	-	bb+	bb	bb	bb	bb-	bb-	b+	b
9	-	-	-	bb	bb-	bb-	b+	b+	b+	b
10	-	-	-	-	b+	b+	b+	b	b	b-

Ratings Detail (As Of October 25, 2021)*

Capitec Bank Ltd.	
Issuer Credit Rating	BB-/Stable/B
South Africa National Scale	zaAA/--/zaA-1+

Ratings Detail (As Of October 25, 2021)*(cont.)		
Issuer Credit Ratings History		
07-May-2020		BB-/Stable/B
26-Nov-2019		BB/Negative/B
29-Nov-2017		BB/Stable/B
02-Jul-2018	*South Africa National Scale*	zaAA/--/zaA-1+
29-Nov-2017		zaAA-/--/zaA-1+
07-Aug-2017		zaAA/--/zaA-1+
Sovereign Rating		
South Africa		
Foreign Currency		BB-/Stable/B
Local Currency		BB/Stable/B
South Africa National Scale		zaAAA/--/zaA-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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