Credit Rating Announcement

GCR affirms Bank Windhoek's and Capricorn's national scale issuer ratings; Outlooks Stable

Rating Action

Johannesburg, 28 September 2021 - GCR Ratings ("GCR") has affirmed the Namibian long and short-term issuer ratings of Bank Windhoek Limited at $AA_{(NA)}$/$A1+_{(NA)}$. At the same time, the South African national scale long-term issuer rating has been affirmed at $A_{(ZA)}$. The outlooks are Stable.

Rated Entity / Issue	Rating class	Rating scale	Rating	Outlook / Watch
Bank Windhoek Limited	Long Term Issuer	National	$AA_{(NA)}$	Stable Outlook
	Long Term Issuer	National	$A_{(ZA)}$	Stable Outlook
	Short Term Issuer	National	$A1+_{(NA)}$	--

Simultaneously, Capricorn Group Limited's Namibian long and short-term issuer ratings have been affirmed at $AA-_{(NA)}$/$A1+_{(NA)}$, with the outlook accorded as Stable.

Rated Entity / Issue	Rating class	Rating scale	Rating	Outlook / Watch
Capricorn Group Limited	Long Term Issuer	National	$AA-_{(NA)}$	Stable Outlook
	Short Term Issuer	National	$A1+_{(NA)}$	

Rating Rationale

Bank Windhoek Limited

Bank Windhoek Limited's ("BW") ratings reflect the credit profile of Capricorn Group Limited ("Capricorn", or "the group"). BW's contribution to group net profit after tax (FY21: 68%) and assets (FY21: 79%) is significant and GCR views it to be the group's core operating entity and flagship brand. As such, the ratings of BW are equalised to the group Anchor Credit Evaluation ("ACE").

The ratings affirmation balances the group's strong and entrenched position as a leading financial services provider in Namibia and good asset quality (although this has weakened from historically strong levels), against adequate funding and liquidity and below peer capitalisation (based on the GCR total capital ratio).

Capricorn Group Limited is a large, diversified financial services company, with core operations in banking (Bank Windhoek and Bank Gaborone (not rated)). The strong competitive position largely pivots on the flagship banking subsidiary, BW, as one of the biggest banks in Namibia, leading the market in credit extension. Diversification comes in the form of high margin, reasonably low risk, micro-lending to government employees (Entrepo), capital-light asset management activities (Capricorn Asset Management) and exposure to insurance through associate shares in the local operations of regional behemoths, Santam and Sanlam. The group also has exposure to telecommunications through its 30% stake in Paratus Group Holdings Limited. The asset manager and insurance associates are clear leaders in their respective markets, and this combined strength supports good, through the cycle revenue stability and diversity, with a high proportion of annuity type interest and fee-based income. There is some geographic diversification from the Botswana banking subsidiary (Bank Gaborone), but the franchise strength of the business is ultimately underpinned by the Namibian operations, supporting the strong competitive position assessment.

Environmental, Social and Corporate Governance ("ESG") considerations are neutral ratings factors, however, we note the group's growing emphasis on renewable energy and sustainable projects through BW, which recently issued the first Sustainability bond in Namibia. Although unlikely in the medium to long-term, should renewable energy projects and broadened focus on sustainable financing become a significantly material component of the bank's loan portfolio, with BW able to leverage off its bond framework and tap further funding for these projects that clearly differentiate it from peers, we could uplift the business profile assessment for ESG characteristics.

We have moderated the risk assessment to reflect the notable upward pressure on asset quality over the last two years. Economic frailties in the group's core market of Namibia, coupled with pandemic-induced disruptions across the region, presented highly challenging operating conditions, which inevitably caused credit losses and non-performing loans ("NPLs") to breach historical levels. That said, BW's asset quality continued to stack up well relative to most peers in Namibia and we do expect a normalisation in key metrics over the next 12-18 months. On the other hand, Bank Gaborone (the smaller banking subsidiary) does exhibit a weaker risk profile than BW, which weighs slightly on overall group asset quality. Looking ahead, we are forecasting contained credit losses of around 0.7% over the next two years (primarily due to normalised provisioning and expected recoveries), but NPLs could remain elevated at just north of 5.6%. While there may be a rebound in economic activity and lower intensity of pandemic effects, there could still be some negative tail impact from significant exposures to vulnerable sectors, such as commercial real estate (c.18% of total advances). This could result in revaluation risk, although provisioning levels (of stage 3 loans) are slightly above most peers, and together with lower interest rates that could support repayment capacity (at least in the short-term), may mitigate some of the pressure on future credit costs.

Like peers, the group exhibits a high reliance on wholesale funding, a structural problem in the Namibian market. BW has the second largest market share of deposits, and the funding mix is fairly well balanced between short, medium and long-term maturities. The GCR stable funding ratio was 85% at FY21, better than most peers. Liquid asset coverage of total deposits was in line with peers at 22%, however, above average loan growth has contributed to a more leverage position, with loans to deposits above 100%. The group continues to hold sufficient liquid assets above regulatory requirements.

Capital and leverage remained quite stable over the past three years, with the GCR total capital ratio around 12.3%. The group is viewed to possess thinner loss absorption buffers, with most peers' GCR total capital ratios tracking above 13%. We believe that there is a high likelihood for earnings improvement over the next two years (following COVID-19 induced earnings strain in FY20) given the expectations for lower credit costs, stabilised net interest margins, moderate loan growth (between 3%-5%) and disposal of the Zambian banking subsidiary (which has been margin dilutive). Our forecast points to a GCR total capital ratio between 12.5%-12.7%, supporting an intermediate capital assessment.

Capricorn Group Limited

The ratings on Capricorn Group Limited are a notch lower than the group ACE, reflecting the structurally subordinated status of Non-Operating Holding Companies ("NOHC"). This reflects GCR's opinion that the NOHC is reliant on cash flows and dividends from largely regulated, operating group companies, which could be interrupted by regulators should there be a stress event.

Outlook Statement

We expect the credit profile of the group to remain anchored by its strong competitive position in the Namibian market, while the recent asset quality pressures are likely to subside over the next two years as credit losses improve to 0.7%. The latter may also support continued earnings momentum, and along with loan growth expectations of 3%-5% and a consistent dividend policy, sustain an adequate, but stable GCR total capital ratio of between 12.5%-12.7% over the rating horizon. We are not expecting a change to the funding structure which aligns to domestic peers, and liquidity is likely to remain adequate with sufficient buffers relative to regulatory requirements.

Rating Triggers

The ratings could be upgraded should asset quality return to historical levels and key capital, funding and liquidity metrics align with/exceed peers. Conversely, negative rating pressure may stem from weakening asset quality, which would weigh on earnings and capitalisation, or any signs of liquidity stress that would undermine the funding and liquidity assessment relative to peers.

Analytical Contacts

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Related Criteria and Research

Criteria for the GCR Ratings Framework, May 2019
Criteria for Rating Financial Institutions, May 2019
GCR Ratings Scale, Symbols & Definitions, May 2019
GCR Country Risk Scores, August 2021
GCR Financial Institutions Sector Risk Score, September 2021

Ratings History

Bank Windhoek Limited (Namibian Scale)

Rating class	Review	Rating scale	Rating	Outlook	Date
Long Term Issuer	Initial	National	AA(NA)	Stable	September 2005
	Last	National	AA(NA)	Stable	September 2020
Short Term Issuer	Initial	National	A1+(NA)	N/a	September 2005
	Last	National	A1+(NA)	N/a	September 2020

Bank Windhoek Limited (South African Scale)

Rating class	Review	Rating scale	Rating	Outlook	Date
Long Term Issuer	Initial	National	A-(ZA)	Stable	November 2013
	Last	National	A(ZA)	Stable	September 2020

Capricorn Group Limited

Rating class	Review	Rating scale	Rating	Outlook	Date
Long Term Issuer	Initial	National	AA(NA)	Stable	November 2015
	Last	National	AA-(NA)	Stable	September 2020
Short Term Issuer	Initial	National	A1+(NA)	N/a	November 2015
	Last	National	A1+(NA)	N/a	September 2020

RISK SCORE SUMMARY

Rating Components & Factors	Risk scores
Operating environment	**11.50**
Country risk score	5.50
Sector risk score	6.00
Business profile	**1.25**
Competitive position	1.25
Management and governance	0.00
Financial profile	**0.25**
Capital and Leverage	(0.50)
Risk	0.75
Funding and Liquidity	0.00
Comparative profile	**0.00**
Group support	0.00
Government support	0.00
Peer analysis	0.00
Total Score	**13.00**

Glossary

Balance Sheet	Also known as Statement of Financial Position. A statement of a company's assets and liabilities provided for the benefit of shareholders and regulators. It gives a snapshot at a specific point in time of the assets the company holds and how they have been financed.
Capital	The sum of money that is invested to generate proceeds.
Cash	Funds that can be readily spent or used to meet current obligations.
Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
Diversification	Spreading risk by constructing a portfolio that contains different exposures whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with as a consequence of holding the security or asset. For a company, its exposure may relate to a particular product class or customer grouping. Exposure may also arise from an overreliance on one source of funding. In insurance, it refers to an individual or company's vulnerability to various risks
Income	Money received, especially on a regular basis, for work or through investments.
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
Issuer	The party indebted or the person making repayments for its borrowings.
Leverage	With regard to corporate analysis, leverage (or gearing) refers to the extent to which a company is funded by debt.
Liquidity	The speed at which assets can be converted to cash. It can also refer to the ability of a company to service its debt obligations due to the presence of liquid assets such as cash and its equivalents. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Long Term Rating	See GCR Rating Scales, Symbols and Definitions.
Margin	A term whose meaning depends on the context. In the widest sense, it means the difference between two values.
Market	An assessment of the property value, with the value being compared to similar properties in the area.
Maturity	The length of time between the issue of a bond or other security and the date on which it becomes payable in full.
Rating Outlook	See GCR Rating Scales, Symbols and Definitions.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Short Term Rating	See GCR Rating Scales, Symbols and Definitions.
Short Term	Current; ordinarily less than one year.

SALIENT POINTS OF ACCORDED RATINGS

GCR affirms that a.) no part of the ratings was influenced by any other business activities of the credit rating agency; b.) the ratings were based solely on the merits of the rated entity, security or financial instrument being rated; and c.) such ratings were an independent evaluation of the risks and merits of the rated entity, security or financial instrument.

The credit ratings have been disclosed to Bank Windhoek Limited and Capricorn Group Limited. The ratings above were solicited by, or on behalf of, the rated entity, and therefore, GCR has been compensated for the provision of the ratings.

Bank Windhoek Limited and Capricorn Group Limited participated in the rating process via teleconference management meetings, and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible. The information received from the entities and other reliable third parties to accord the credit ratings included:

- Audited financial results as at 30 June 2021;
- Other publicly available information and
- Industry comparative data.