FINANCIAL DERIVATIVES COMPANY LIMITED

Volume VI, Issue 64

February 8, 2016

FDC ECONOMIC MONTHLY

VAT IN NIGERIA: THE ECONOMIC IMPACT OF AN INCREASE

INSIDE THIS ISSUE:

INTRODUCTION

With the persistent fall in the price of crude oil, Nigeria has been plunged into an economic downturn that has left the government desperately looking to other sources for revenue generation. Oil accounts for over 75% of government revenue and 90% of export revenue and has fallen to levels below $35 per barrel. Compared to the glory days of $100 plus oil prices, this is a 70% decline in prices and has been accompanied by a 27% fall in foreign direct investment. These declines have had profound implications for the nation’s revenue foreign reserve, public expenditure and economic growth. Specifically, the 2016 budget had planned a N2.22 trillion deficit with a benchmark oil price of $38/barrel. With the current realities of oil falling below $30/barrel, there is a much larger deficit to accommodate.

In addition to the decline, the U.S. lifting of Iran's economic sanctions is a further threat to Nigeria. Iran, which has the fourth largest oil reserve in the world (160 billion barrels), is now poised to export oil to the international oil market, and has recently announced it can produce oil at $1/barrel. This means Iran can afford to sell its oil below the official international rate if it pleases, which would further hamper Nigeria's export efforts and revenue expectations. Other key challenges include the declining stock market, the increasing inflation rate (currently at 9.6%), the exchange rate volatility, and declining oil reserves, a problem which has prompted the Central Bank of Nigeria (CBN) to take several measures to defend the value of the naira.

As a result, it has become imperative for the government to diversify the economy and increase revenue generation from other sources. Tax increases have been one of the front-line considerations, with an increase in VAT among the options.

VAT IN NIGERIA

Value-Added Tax (VAT) is a tax on consumer spending. It is payable on goods and services consumed by any person whether government agencies, business organizations or individuals.[1] It can also be defined as a tax on spending/consumption levied at every stage of a transaction but eventually borne by the final consumer of such goods and services. In Nigeria, it is levied at a flat rate of 5%. VAT is collected on behalf of the government by businesses and organizations which have registered with the Federal Inland Revenue Service (FIRS) for VAT purposes.

ECONOMIC IMPACT OF VAT INCREASE: PROS AND CONS

An increase in VAT has been one of the forefront considerations of the Federal Government in recent times to increase its revenue stream. During the four day visit of the International Monetary Fund (IMF) to Nigeria in January 2016, the managing director of the IMF, Ms Christine Lagarde, called for an increase in VAT describing it as the lowest in the ECOWAS region and one of the lowest around the world.[2] The VAT rate is low compared to 19.25% VAT paid in Cameroon, 14% paid in South Africa and 17.5% in Zambia. In Egypt, 10% is charged on standard goods and services while 25% is charged on luxury items and zero on exports. VAT in Kenya ranges between 12-16% while in India, it is between 5.5% and 14.5%.[3] As such, there is precedence for an increase. However, the implementation of such a decision would need to be carefully considered.

1 Vanguard News – Value Added Tax (VAT) in Nigeria. 20 January 2016. http://www.vanguardngr.com/2015/05/value-added-tax-vat-in-nigeria-i/

2 Daily Trust News. 20 January 2016. http://www.dailytrust.com.ng/news/general/christine-lagarde-in-nigeria/128024.html#UluW4Q3cKwx3sp2H.99 .

3 Leadership News. Available from: http://leadership.ng/business/454222/100-vat-increase-good-policy-inappropriate-timing. [25 January 2016]

Nigeria has one of the highest poverty rates in the world and an increase in a consumption tax like VAT would be a huge burden on the average Nigerian. In terms of income distribution, Nigeria is among the most unequal countries in the world. The increase will therefore shrink the purchasing power of the already impoverished Nigerian income earner. The unemployment rate in Nigeria is expected to rise to 10.5% by the end of the first quarter of 2016, from 9.9% in Q3'2015 according to the Trading Economics global macro models and analysts' expectations[4]; and inflation which has also been on a steady increase since 2015 currently stands at 9.6%. An increased VAT will consequently increase inflation rate, as businesses will see it as an excuse to raise prices of goods and services arbitrarily.

Also, the GDP annual growth rate at 2.84% in the third quarter of 2015[5] showed a decline in economic productivity from previous level of 6.23% in the third quarter of 2014, and cannot support a VAT increase. All these macro-economic variables suggest that a VAT increase is not a welcome financial burden that Nigerians will be willing to take on.

On the other hand, a VAT increase would increase the government revenue stream, which can be invested in infrastructure, other developmental projects, and stimulate economic growth. The additional revenue would help reduce government's dependence on oil revenue. Whilst this is good, the immediate increase could reduce overall consumption and further slow-down the economy making it counter-productive.

If a VAT increase were to be implemented by the government, several measures should be taken to ensure that the objective of the increase is obtained. An instance is the provision of the relevant technology to ensure proper monitoring, collection and elimination of leakages. The VAT increase could be varied relative to kind of the goods/services being purchased, since the effect on the poor would be greater than on the rich. e.g. higher VAT rate on luxury items. Transparency, accountability, and proper sensitization of the masses on the need for an increase are also required. Since the plan of the government is to borrow to fund part

4 Trading Economics – Nigeria Unemployment Rate. 02 February 2016. http://www.tradingeconomics.com/nigeria/unemployment-rate/forecast

5 Trading Economics – Nigeria's GDP Annual Growth Rate. 02 February 2016. http://www.tradingeconomics.com/nigeria/gdp-growth-annual

of the budget, the borrowing if judiciously implemented would help stimulate the economy, giving room for the government to gradually increase taxes like VAT.

CONCLUSION

Nigeria's VAT rate at 5% is beyond doubt one the lowest in the world. It can therefore be argued that VAT should be increased, however with the current rate of poverty in Nigeria and the present economic situation, an increase in VAT would pose a huge financial burden to the average Nigerian. Rather than an increase in VAT at this time, other avenues could be explored in the short term such as the absolute removal of petroleum subsidy which many have argued does not benefit the Nigerian populace. The plugging of fiscal leakages, a move which is currently being enforced by the present administration, can also be further strengthened.

Even though a VAT increase may at some point be unavoidable, now would be a bad time for an increase.

HEADLINE INFLATION RATE TO DECELERATE MARGINALLY TO 9.5%

We are projecting that YoY headline inflation will decline marginally to 9.5%. This will be good news to the CBN, who at the last MPC meeting said "the Committee would continue to monitor consumer price developments with a view to formulating policies that will keep inflation in check". This decline will be contrary to the annual trend in 2014 and 2015, when the price level increased in January.

INFLATION COULD BECOME STRUCTURAL

The jury is out as to whether the current inflationary trends are transient or embedded. Our view is that the underlying headline inflation movement is a combination of factors, mainly cost-push. The slowdown in inflation in January can be partly attributed to the cumulative effect of a reduction in aggregate income and demand, following a contraction in government spending. One of the key variables that drive costs of goods is the price of diesel which is used for the transportation of food items from the farms to the urban markets. In January, the price of diesel declined sharply from N135 to N114. There has also been reduced demand following the end of seasonal festivities. January is also the month school fees are paid. These factors combined have further reduced discretionary income. Furthermore, though the scourge of imported inflation persisted due to record weak levels of the naira (as weak as N307/$), the intensity of imported inflation was abated by pushback from consumers who either have cut demand or use cheaper substitutes. Products with a high elasticity of demand such as air travel have been affected by lower demand due to increasing costs. Given persistent macroeconomic headwinds, which have led to lower disposable income and a bleak outlook, consumers have generally cut back spending on food and non-food items.

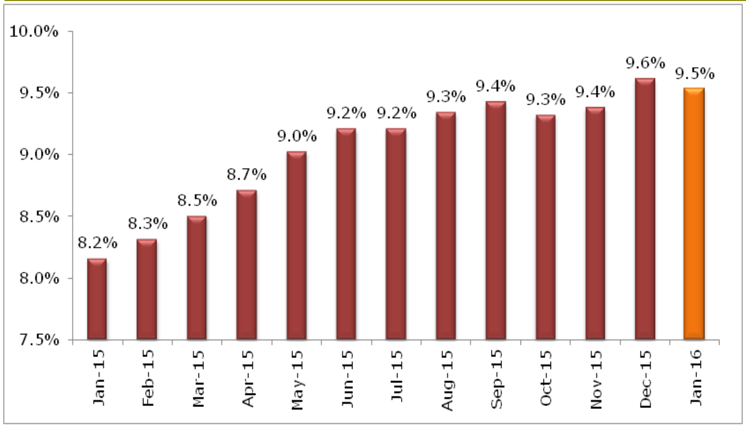
INFLATION LIKELY TO SPIKE AGAIN IN MARCH

In the short-term, the increased electricity tariff will increase costs to artisans but will have no significant impact on prices. Planting preparations towards the end of Q1 are also expected to push food prices higher. The real catalyst for inflation is the exchange rate effect which is already being felt. The Financial Times in its article titled “Nigeria’s poor feel the pain of Abuja’s monetary policy” said that “a vendor...reports that she sells 3 cubes for 10 naira. Less than a year ago, the 10 naira note bought 4 cubes”. Finally, with the FGN set to pass the 2016 budget by the end of February, government spending will also likely add to an increase in inflation in the coming months.

REGIONAL INFLATIONARY TREND

In SSA, inflation has remained muted. In some cases, prices have actually declined. We attribute this to the falling price of oil. Most African countries are oil consumers. At 9.5%, Nigeria will rank number 13 amongst countries with the highest inflation rate in Africa. Kenya’s inflation rate slowed to 7.8% in January 2016 compared to 8% in December 2015. This decrease in inflation rate was due to the slow down in prices of transportation, housing, food and non-alcoholic beverages. Furthermore, Uganda’s inflation rate decelerated to 7.6% in January 2016 compared to 9.3% in December 2015. The decrease in Uganda's inflation was as a result of the fall in the prices of food crops, energy, fuel and utilities.

Chart 1: Headline Inflation Rate



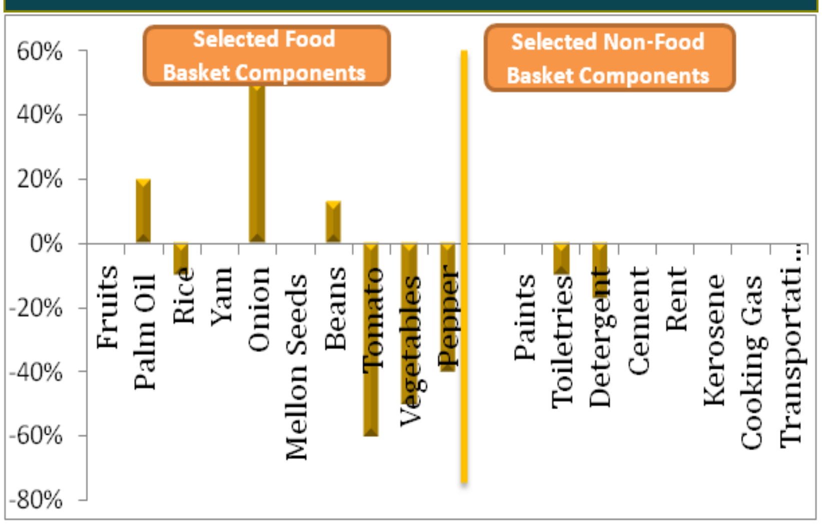
Source : NBS, FDC Research

URBAN PRICES DECELERATED IN JANUARY

The FDC Lagos urban inflation index decreased significantly by 1.83% to 10.53%. This decrease in urban inflation was driven by the huge decrease of 4.76% in the food index.

The year-on-year (YoY) food index decreased to 11.36% from 16.12%, while the YoY non-food index decreased to 10.11%, from 10.45% in December. Food prices decreased in January as demand fuelled by year end festivities waned. We expect the impact of the new electricity tariff to reflect in February's urban inflation.

Chart 2: FDC Urban Index



Source : FDC Research

Likely Market Response

Interest Rates

Given the CBN's decision to retain the MPR, interest rates in the money markets are expected to remain low. However, in the medium term, increased government borrowings are expected to spur an uptick in money market rates.

External Reserves

Nigeria's external reserves are approximately $28bn. As exchange rate pressures persist and oil prices remain low, Nigeria's external reserves are expected to dwindle further.

Stock Market

Stock market activities are expected to be driven by earnings announcements which investors anticipate soon.

THE NIGERIAN MINING INDUSTRY, THE UN-TAPPED GOLDMINE

The Nigerian economy has remained susceptible to the swings in the global energy market for over fifty years. With crude oil accounting for approximately 70% of government revenue and 83% of export earnings, Nigeria is forced to make difficult adjustments almost every time there is a depression in oil prices. This situation is compounded by corruption, and the poor management skills of economic managers. There has been several calls for the diversification of the economy but nothing significant has been done. Now that we are at the trough of the economic cycle, and with a new government at the helm of affairs, it is imperative for us to put on our thinking caps to explore alternative sources of growth.

Nigeria is richly endowed with mineral resources that are yet to be explored. In 2014, solid minerals accounted for about 0.14% of the GDP, significantly lower than the 10.44% contributed by oil and gas. The Nigerian Extractive Industries Transparency Initiative (NEITI) carried out an audit in 2012 which revealed that Nigeria has over 40 different kinds of latent solid minerals and precious metals. According to the report, 70% of the mineral endowments are located in the northern part of the country. The paradox is that the north is also the most impoverished region in the country.[6] Investments into the mining industry would not only diversify the economy away from oil and gas but would also ensure investment into this extremely impoverished region.

NIGERIA'S SOLID MINERALS AND THEIR ECONOMIC VALUE

The solid minerals available in commercial quantities in Nigeria include coal, columbite and tantalite, limestone, tin ore, gold, lead and zinc amongst others. Our focus will be on the economic value of columbite/tantalite, coal and tin ore.

6 NEITI. 2012. "EITI IMPLEMENTATION: APPLICATION OF EITI TO THE SOLID MINERALS SECTOR IN NIGERIA" http://neiti.org.ng/index.php?q=events/2012/mar/papers-presented-neiti-national-conference

- **Columbite and tantalite*:*** These minerals are found in Plateau, Kano, Kaduna, Bauchi, Kogi and Nassarawa states. Columbite and tantalite are substitutes for one another. They are major components used in the production of condensers and micro-electronic technology (chips and processors), cell phones and nuclear reactors. They are also used as an alloy of steel to form weldable high speed steel for radio transmitting valves and heat sensitive detective devices. A research carried out by Foraferam has shown that the return on investment (ROI) on columbite and tantalite ore is between 10 – 15% and China is a major market for tantalite, where it is being sold at about $122.40/kg.[7] If Nigeria could rally investment around the 14,233 tons of proven reserves, columbite and tantalite mining could be worth $1.74bn to the Nigerian economy.

- **Coal*:*** Coal production in Nigeria dates back to 1909 when it was first discovered in Enugu. Commercial production commenced in 1919 and reached its peak of about 583,425 tons in 1950, with reserves across Delta, Kogi, Ondo, Plateau, Bauchi, Kwara and Nassarawa, in addition to Enugu. However, the outbreak of war in 1967 resulted in the abandonment of most of the mines and the sector has never recovered. Coal is mainly used for power generation and production of steel. Coal fired plants accounts for about 41% of global electricity output while 70% of global steel production is from coal. With huge coal reserves in Nigeria, at about two billion metric tons, the country has the potential to address its chronic power challenge while also meeting the demand of neighbouring countries in the African region, and the significant demand from China, which accounts for about 50% of the world demand. The commodity is currently trading at $43.50/ton, which would value Nigeria's estimated two billion metric tons at $87bn.

7 Foramfera. 2012. "Tantalite ore export in Nigeria non-oil export opportunity in Nigeria" http://www.foramfera.com/index.php/market-research-reports/item/147-tantalite-ore-export-in-nigeria-non-oil-export-opportunity-in-nigeria

MHF PROPERTIES LIMITED

"Where Quality Living Exceeds Expectations"
3B Osborne Road, Ikoyi, Lagos, Nigeria
01- 8418662, 0802 342 3874, 0705 400 6101
info@mhfproperties.com
www.mhfproperties.com

A MEMBER OF THE DANGOTE GROUP

FOR LEASE

MARIYA COURT

Location: 2B, Probyn Close, Ikoyi, Lagos

Amenities:

1. All rooms fitted with new air conditioners
2. Intercom system
3. Equipped kitchen with electrical cooker/oven, fridge, deep freezer and washing/drying machine.

Other Facilities:

1. Gym, squash court, steam bath, sauna, swimming pool with bar and barbeque stand
2. 24hrs power supply
3. 24hrs security/CCTV/Alarm system
4. 24hrs Technician on duty
5. Fully equipped play area for children

RHAMA GARDEN

Location: 28, Gerard Road, Ikoyi, Lagos

Amenities:

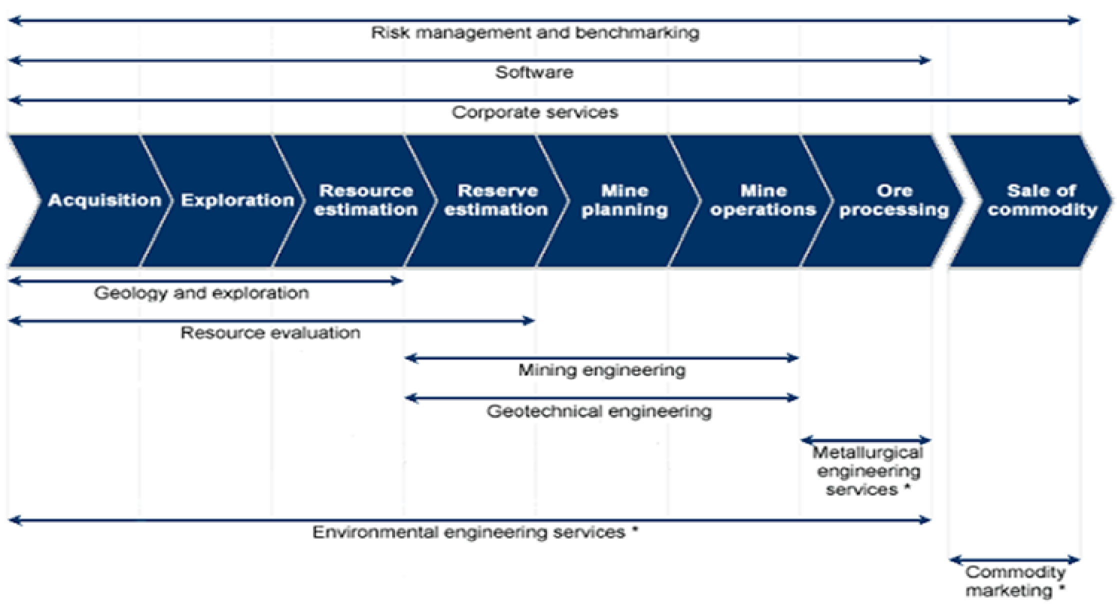
1. All rooms fitted with new air conditioners
2. Intercom system
3. Equipped kitchen with electrical cooker/oven, fridge, deep freezer and washing/drying machine.

Other Facilities:

1. Gym, squash court, steam bath, sauna, swimming pool with bar and barbeque stand
2. 24hrs power supply
3. 24hrs security/CCTV/Alarm system
4. 24hrs Technician on duty
5. Fully equipped play area for children

- **Tin Ore:** Plateau State is endowed with a significant quantity of tin ore, which is used to create bronze, a water-resistant metal alloy. The metal is receptive to polishing and used as a protective coat for other metals. Accordingly, it has huge economic value as it is used in the production of tin oxide resistors, paint, electric lead wires, paper and ink industries. However, low investment and fragmentation plague the sector, which is also riddled with illegal mining activities and poor regulatory oversight. According to Foreminifera market research, the return on investment on the export of tin ore is estimated between 10-15%.[8] The commodity is currently trading at $6.07/lb, which would value Nigeria's proven reserves of 10,546 tonnes at roughly $141mn.currently trading at $6.07/lb, which would value Nigeria's proven reserves of 10,546 tonnes at roughly $141mn.

THE MINING SECTOR VALUE CHAIN



Source: African Partner. 2004. "The mining industry value chain" http://www.africanpartner.com /image/services01.gif

8 Foramfera. 2012. Tin ore cassiterite export in Nigeria non-oil export opportunity in Nigeria http://www.foramfera.com/index.php/news-and-press-release/item/149-tin-ore-cassiterite-export-in-nigeria-non-oil-export-opportunity-in-nigeria

IMPERATIVES FOR THE DEVELOPMENT OF THE MINING SECTOR

In spite of the obvious economic value in the solid mineral sector, challenges have continued to hamper the sector's development and growth. The effects of these are evident in the high rate of inefficiencies, which have cost implications and are reducing the country's competitiveness in the global market. According to the World Economic Forum, Nigeria ranked 127 out of 144 countries in the 2014/15 Global Competitive Index. Key challenges include: infrastructure, financing, security and regulation.

- **Infrastructure*:*** The high infrastructure deficit in the country has implications for the cost of logistics in the sector. Nigeria's infrastructure deficit is estimated at $300bn. As most of the solid minerals are located in the Eastern and Northern regions of the country, an efficient and effective rail network is required to facilitate competitive mineral exports. Poor power supply is also taking its toll on the cost of mining as the mines have to self-generate their power. However, we expect that the Buhari government's commitment to infrastructure financing will positively impact this strategic infrastructure. The 2016 budget shows that the government has earmarked N1.85trn for capital expenditure, 230.36% higher than the N560bn expended in 2015. There has been improvement in power output in recent times, which is attributable to the privatization of the power sector and increase in gas supply. We expect this performance to be sustained through the financial support by the CBN, the increase in power tariffs and effective regulatory oversight. Accordingly, the outlook for infrastructure development in the country looks positive.

- **Financing*:*** The mining sector is capital intensive and requires long term investments. Macroeconomic stability and clarity of policy are key to attract the required investments. The uncertainties witnessed in recent times has seen net foreign direct investment plunge from a high of $8.1bn in 2011 to $1.6bn in 2015, hence the need for the government to be articulate about its policy direction. The active participation of the government will also encourage the banks to lend to potential investors. The Bank of Industry in Nigeria has promised to disburse a loan estimated at N24bn to entrepreneurs willing to invest in the solid minerals sector. Accessibility to long term financing is a prerequisite for adequate investment in capital expenditure while commercial banks may be required to bridge the short term funding gaps. The CBN has continued to advocate that commercial banks should lend to the solid mineral sector. We expect to see inflows of investment into the sector in the medium to long term.

- **Security*:*** Insurgency and kidnappings are of major concern to investors and expatriates. This distorts activities and increases the cost of doing business. The commitment of the new government to tackle insurgency through increased and effective funding of the military is positive, alongside the significant drop in the rate of attacks by Boko Haram. Similar commitments have been made by the Buhari administration with regards to kidnapping and initial steps to better arm and equip security operatives at the state level are beginning to yield results. This is a welcome development and has been commended by the global community. The expected improvements to the security situation will boost investor perception of the country and attract more foreign direct investment (FDI).

- **Regulation:** A dynamic regulatory environment is vital to attract the required investment into the sector. With the changing fundamentals in the global commodity markets, it is necessary that the government review the 2007 Mining Act to reflect the new market realities. Commodity prices are currently depressed due to the oversupply in the market. The Bloomberg Commodities Index has declined by 27.98% year-on-year. Price competitiveness is an imperative globally. Some of the changes the government may consider include the downward review of the current royalties and taxes so as to enable the producers to breakeven and price their commodities competitively. The Minister of Mining has been advocating for inclusive participation by all the stakeholders including the legislators in order to revamp this moribund sector. With mining being a major pillar of the current administration, we ex-

The Address Homes
Femi Okunnu, Lekki

30 Beautiful comptemporary, 4 Bedroom Luxury Semi-detached Homes, with 1 Bedroom BQ on 3 floors, where intelligent design meets aesthetics to create the perfect backdrop for the modern lifestyle. Located at Femi Okunnu Estate, close to the new Shoprite, Lekki, Lagos.

Come home to exceptional quality living with designs to maximize comfort and convenience, specifications that include: Master Bedroom on 2 floors with Wardrobe in Alcove and beautiful staircase with Lovely overlooking gallery; modern and contemporary fully fitted kitchen with Breakfast Island; Interior Spaces with Sun lit space all day long, modern interiors, height windows bringing in lots of natural light and ventilation, floor to ceiling Doors, Double/triple volume spaces, Bridges, Split-level ceilings, Atrium creating an interior lantern for ventilation and lighting, Galleries and interconnecting levels, Smart Technology for intelligent living; Integrated music system pre-wiring; Integrated CCTV pre-wiring; Intercom system in all functional rooms pre-wired; DSTV in all rooms; Mood lighting, 4-parking spaces; Outdoor energy efficient lighting on building and more.

Inclusive of Communal Swimming Pool, Club House, Mini Event Centre, Children Play Area, 24Hrs Power Supply, Adequate Security, Central Sewage Disposal System, Good Drainage and Landscaping. Fully serviced Estate.

CONSTRUCTION ON GOING

For enquiries call:

Dimeji - 08069402201, Dami - 09038859470, Doyin - 07061539863, Temitope - 08021170082, Eddy - 08033047772

Main Arterial Road
(Beside RCCG Olive Tree Parish),
Off Onikoyi Street, Banana Island,
P.O. Box 55500, Ikoyi, Lagos.
0806 940 2201, 0909 040 6925, 0903 885 9470
info@theaddresshomes.com
www.theaddresshomes.com

TheAddresshomes @theaddresshomes @theaddresshomes pect the passage of investor friendly laws that will enhance its attractiveness.

Despite the fact that Nigeria is well endowed with these natural resources, it remains one of the poorest nations in the world. There is no better time to take the relevant fundamental decisions that will steer the economy back to the path of growth and stem the looming social crisis. The change in the country's export base will reduce its exposure to exogenous shocks, lower its unemployment rate, increase government revenue and boost the value of the naira.

The Minister of Solid Minerals, Dr Kayode Fayemi, has solicited for state governments to establish investment vehicles either wholly owned by the states or in partnership with the private sector through which they can exploit the solid mineral deposits in their states. This is a step in the right direction and should translate in an increase in investment and activity in the sector. The plan to increase investment in infrastructure from about 15% to 30% of budget will also create an enabling environment required to support the sector. There is no better time to revamp this abandoned jewel than a time like this when the downward pressure on the oil price has negatively impacted on the hydrocarbon sector.

OF FINES AND THE NIGERIAN BUSINESS ENVIRONMENT

The business environment in Nigeria can best be described as a jungle: survival of the fittest, winner takes all. In the past, a lax regulatory environment encouraged business entities to take advantage of consumers and even to cannibalize competition. Fast forward to post election 2015 and the regulators seem to have jumped into action. From the banking sector where the Central Bank of Nigeria (CBN) and the Federal Reporting Council (FRC) have fined erring banks billions of naira for Treasury Single Account (TSA) lapses and poor reporting standards, to the telecommunication sector where the National Communication Commission (NCC) has dished out some heavy fines to National Food and Drug Administration and Control (NAFDAC) and its sudden love for hygiene controls, the message seems clear: Fall in line or get whopped. The ultimate beneficiaries of this new regime are the government and citizens of Nigeria. While several bodies have called out the Nigerian government for issuing excessive fines to raise an ambitious budget of N8.5 trillion in the face of dwindling oil revenues, one cannot help but wonder why organizations (both local and foreign) operate with so much disregard for the mandates of the government, while they adhere strictly to the laws of other nations where they operate. In short, while there is no doubt that fines should be disciplinary, and not punitive in nature, enforcement must also follow to avoid the flagrant disregard for regulation that Nigeria has witnessed in years past.

FINES WITHOUT ENFORCEMENT

In 2014, for example, Coca-Cola was indicted for failing in its responsibilities to the Nigerian consumers and fined N100million. There was a flagrant disregard for the orders of the council and the office of the Attorney General of the Federation had to intervene and call the organization to order. By implication, Coca-Cola is indifferent to the standards set by the regulatory body and showed no remorse for its actions either.

At about the same period last year, the National Food and Drug Administration Control (NAFDAC) slammed a fine of N1billion on Guinness Nigeria for using expired raw materials for production. Guinness Nigeria has also gone to court and is yet to pay the fine.

The story is same for Stanbic IBTC, which is also challenging the N1billion levied on it by the Federal Reporting Council (FRC) in court. It is interesting to note that foreign companies are quick to run to court in a bid to subjugate the efforts of the regulators.

FINES IN EXCESS

However, it is also imperative that we consider the short and long-term effects such fines have on the business environment. Last October, the Nigerian Communications Commission (NCC) fined MTN $5.2billion for failing to disconnect 5.2 million unregistered SIMs on its network. MTN Nigeria's total revenue in 2014 was $2.6billion. In effect, the fine was two times the company's annual profit in 2014. The fine sent shock waves around the business world and reverberated particularly in South Africa where the company is headquartered. Although the fine was reduced to $3.9billion, three months later, the company is yet to pay the fine and has dragged the NCC to court.

Excessive fines that are not properly enforced sends out mixed signals to both local and foreign investors. Foreign investors who wish to do business in Nigeria get to hear of these fines and become hesitant. For investors already in Nigeria, it is an indication that they can go and act as they wish without regard to the laid down laws knowing fully well that they can take advantage of a weak judicial system to get away with their misdeeds.

As the government tries to woo foreign investors to come and do business in Nigeria, there is a need to ensure that the business environment is made conducive

LONG TERM EFFECTS

Only last week, South Africa announced that it may soon stop buying crude from Nigeria following the lifting of sanctions on

Iran. Conspiracy theorists say its retribution for the fines levied on its business in Nigeria. It may sound far-fetched, but it is indeed plausible. According to the EIU, Foreign Direct Investments (FDI) was as high as $8.1billion in 2011 and fell to $1.4billion in 2014 down by over 82%. FDI has crashed to almost zero in the last few months. With the current posturing by the new administration, a net reversal of FDI's is imminent.

Fines should be more disciplinary than punitive. There should also be some form of enforcement of these fines so defaulters do not take them for granted. Regulators on their own part need to be more proactive than reactive as their primary purpose is to standardize and not to drive revenue.

Nigeria's business environment is already perceived as being a volatile investment destination and any indication that the country sees fines, as an avenue to generate revenue will do more harm than good.

Fidelity

Supporting The Economy In Tough Times?

It's A Tough Job - But Somebody's Got To Do It

Building an economically strong nation is a partnership - one to which we are fully committed.

We're Fidelity, we keep our word.

#ToughJob

Contact Us: +234(1)448-5252, +234 8003-433-5489 true.serve@fidelitybank.ng

WAYS TO BANK WITH US

Branch | ATM | Online Banking | Mobile Banking | True Serve

Fidelity Bank Plc

RC 103022

FOLLOW US:

www.fidelitybank.ng

7EVEN INTERACTIVE

aaan/0046

GLOBAL PERSPECTIVE – OIL: FROM BOOM TO BAILOUT? - CULLED FROM THE FINANCIAL TIMES

CHEAPER CRUDE MEANS MANY DEVELOPING COUNTRIES WILL TAKE LONGER TO CATCH UP WITH ADVANCED ECONOMIES

Since the start of the 21st century the South American nation of Suriname, population 540,000, has been riding a commodity boom that yielded major benefits for a country rich in bauxite, gold, oil and bananas.

From 2000 to 2014, annual per capita income more than quintupled to almost $10,000. Child mortality fell by a third. A child born there today can expect to live to 70, up from 67 just 15 years ago.

In January, however, the government of former military ruler Dési Bouterse, who remained president following a democratic election last year, had to confront a harsh reality. After watching foreign reserves more than halve last year, it asked for help from the International Monetary Fund, the World Bank and other institutions, whose representatives are due to land in the capital city of Paramaribo next week.

With that move, Suriname set out on a path to an international bailout. More countries whose economies depend on exports of oil and other commodities may follow suit, punctuating the end of the "supercycle" that lifted their fortunes for years.

Asked recently what kept her up at night, Christine Lagarde, managing director of the IMF, says she worries about the fate of low-income oil producers like Nigeria.

"That's a country that is facing, like many other oil-producing countries, a real hardship and a necessity to very promptly redesign its business model and realign its interests with a completely new reality which is here for longer than many think," she said.

The concerns at the IMF go beyond the effect on budgets and growth and fears over a balance of payments crisis.

IMF economists warned this week that commodity price shocks could weaken banks in developing economies, raising the prospect of a commodity-driven financial crisis. Others worry about the impact on markets of oil-fed sovereign wealth funds selling down assets to cover for declining oil revenues.

Nigeria has so far avoided going to the IMF, though a growing number of analysts think it should. It is in discussions with the World Bank and other institutions about borrowing billions to plug a $15bn budget deficit left by falling oil revenues. Azerbaijan has also had discussions with the IMF and World Bank about a $4bn loan package.

There are concerns inside the IMF and World Bank that others, like Ecuador and even Venezuela, could be seeking bailouts before long. Across Africa some observers foresee low-income oil producers from Angola to Gabon being forced into bailouts.

Major emerging economies like Brazil and Russia seem safe for the time being thanks to their foreign exchange reserves, but such confidence will erode if commodity prices stay low into next year and deplete reserves. Moscow is already considering the privatisation of trophy assets such as airline Aeroflot and oil group Rosneft to fill the gap left by falling oil revenues.

Kaushik Basu, World Bank chief economist, argues that the collapse in commodity prices is likely to create a split in the global economy and among emerging economies. It also comes as the slowdown facing emerging economies like China is curbing the rate at which they catch up with advanced economies. The IMF says it expects that "convergence" will happen at less than two-thirds the rate it did previously.

Cheap oil is still a boon to many developing countries, including India and Bangladesh, and advanced economies such as the US, where consumers have gone on a car-buying binge fuelled by falling fuel prices.

Yet most economists have been too slow to recognise the potential for damage to producers in the developing world. "I have to admit [the fall in prices] has gone on longer than I or we anticipated," Mr Basu says. At the IMF and World Bank, economists now expect the slump in commodity prices to endure for some time. They argue that other developing producers are going to have to rush through painful budget adjustments.

In January, the World Bank slashed its 2016 forecast for crude prices to an average of $37 a barrel, down from $51 a barrel in October. That came alongside a broader rethink of the direction of commodity prices, with the bank's economists lowering their forecasts for 37 of the 46 commodities they track.

The problem, says Mr Basu, is that too many producing countries are in denial about the shift or the potential remedies — and are afraid of the political consequences. "It will be very difficult. There's no getting away from it," he says.

Even in Suriname policymakers were until recently in denial. When the central bank announced a 25 per cent devaluation against the dollar in November it did so with a terse statement: "Suriname is momentarily experiencing a genuine commodity shock."

Six weeks later that shock looks far from momentary with tough-minded negotiations with the IMF, World Bank and other institutions about to get under way. The question is which countries will turn to them next?

CASE STUDY: RUSSIA

Sergei Glazyev has radical recipes for dragging Russia out of its crisis. The maverick economist and adviser to President Vladimir Putin wants to fix the rouble's exchange rate and dish out Rbs5tn ($66bn) in loans to Russian companies.

Despite Moscow's combative rhetoric, Mr Putin tends to follow the prudent advice of Elvira Nabiullina, the central bank governor, instead of radical ideas like Mr Glazyev's. Still, the economist's proposals highlight the pain of cheap oil.

Russia is set to undergo a second year of recession after its economy contracted by 3.7 per cent in 2015. The government is seeing its coffers drained as oil and gas revenues, which accounted for 43 per cent of the budget last year, are forecast to sink to under 35 per cent this year.

The finance ministry is seeking up to Rbs1tn in additional revenues to keep the budget deficit at 3 per cent. Mr Putin is considering the sale of stakes in state enterprises to raise funds.

One obvious source for additional funds is the oil sector itself. Already last year, the government raised Rbs200bn from the sector by keeping export duties at 42 per cent rather than cutting them to 36 per cent as planned. Oil executives fear the government could keep the tax at 42 per cent indefinitely, which VTB Capital says may cut the sector's value by 20-30 per cent. Consumers are suffering, too. Pensions were raised by only 4 per cent this month to make up for rising prices, just one-third of the inflation rate.

The rapid fall of the rouble has prevented the central bank from lowering high interest rates. Last week, the bank held rates steady and even indicated that it could raise them to rein in inflation.

As a result, many companies cut investment and consumers tightened their purse strings. Retail sales plummeted by more than 15 per cent in December, the steepest monthly decline since the contraction began in late 2014.

Yet things could have been worse. "Given the magnitude of the oil price shock and the nearly complete lack of access to global financial markets, the Russian economy proved quite resilient in 2015," says Sberbank CIB.

CASE STUDY: NIGERIA

Will low oil prices finally push Nigeria, Africa's top crude producer, to enact reforms that make it less vulnerable to future shocks?

If the past is any indication, no. But President Muhammadu Buhari's government says change will be painful but is possible — and the only choice.

With oil prices having hit a 13-year low in January, the high times that Nigeria enjoyed for the past decade or so are over. The IMF predicts growth will be 3.25 per cent this year, down from an average of 6.8 per cent in the 10 years to 2014.

The country has been here before, on the watch of Mr Buhari, a former army general who came to power by a coup more than 30 years ago during a downturn. He was overthrown after 18 months by officers who accused him of failing to kick-start the economy.

Capital controls introduced by the central bank, and heartily endorsed by Mr Buhari, are hurting the economy and choking the foreign exchange market in this imports-dependent country of more than 180m people. On the black market, the naira has been trading at nearly a 50 per cent premium to the official rate, hurting the poorest citizens most.

Some analysts are concerned by Nigeria's talks with the World Bank and African Development Bank over $3.5bn in loans to plug part of a $15bn gap left by lost oil revenue. But the move could be a sign of a more realistic approach than Nigeria has taken in many years. The bid to borrow cheaply for badly needed basic infrastructure projects could help the administration diversify from oil and revive manufacturing and agribusiness.

In the proposed 2016 budget, Abuja will receive just 20 per cent of total revenues from oil — down from more than 70 per cent. The benchmark price of $38 a barrel is also realistic, analysts say. The target of increasing revenues from sources other than oil could be achievable, partly because Nigeria is starting from a low base but also because Mr Buhari is running a tighter ship.

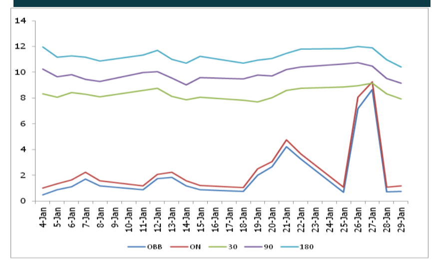
“If they can increase tax revenues, plug some leakages and cut costs they can shift the dial to a more positive place,” says an international investor with interests in Africa

MACROECONOMICS INDICATORS

MONEY MARKET

The opening liquidity position in the money markets was considerably lower in January relative to the prior month. The markets opened at N460.52bn on the 29th of January, 51.82% lower than December's position, which was N955.82bn long. The decrease in liquidity was as a result of the monetary authority's decision to mop up excess liquidity by lifting the suspension on OMO auctions initiated in October 2015.

Chart 3: NIBOR % p.a.



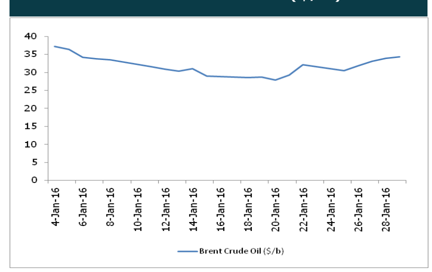
Source: FMDQ, FDC Research

Short term interbank rates averaged 4.36% p.a. in January, 74bps higher than the corresponding period in December. Interest rates moved in tandem with market liquidity. Specifically, the OBB and O/N rates, which opened at 0.5% p.a. and 1% p.a., increased to a high of 8.67% p.a. and 9.25% p.a. respectively, before closing the month of January at 0.75% p.a. and 1.17% p.a., 25bps and 17bps higher than their respective figures in the previous month.

Outlook

We expect interbank rates to continue to move in tandem with liquidity conditions in the market. The CBN is expected to continue with its intervention measures to manage liquidity in the markets. The receipt of the miniature monthly statutory funds of N387bn is expected to push interest rates down slightly pending an ejection of a significant amount from the markets.

Chart 4: Brent Crude Oil ($/b)



Source: Bloomberg, FDC Research

OIL MARKET

Oil Prices

Global oil prices (Brent crude) averaged $31.90pb from January, 2016, 18% lower than the average of $38.90pb in the corresponding period in December. Oil prices trended lower as a number of supply and demand shock events which occurred during the month of January weighed on prices. Western powers lifted sanctions imposed on Iranian crude trade, Iraq is producing at record high of 4.13mbpd and US shale producers have remained resilient despite the decline in oil prices. Although, geopolitical tensions arose between Middle Eastern Oil giants (i.e. Saudi Arabia and Iran), it was not enough to submerge the oversupplied market.

Outlook

The outlook on oil prices remains bearish as crude prices are unlikely to rebound with slowing demand from emerging economies such as China, increased production from Non-OPEC producers and an inability for Oil producers to co-ordinate production to bolster prices. This has significant implications for Nigeria's budgetary framework which is premised upon a benchmark oil price of $38pb. If oil prices persist in the current downward path, Nigeria's fiscal deficit may widen further due to revenue shortfalls.

OIL PRODUCTION

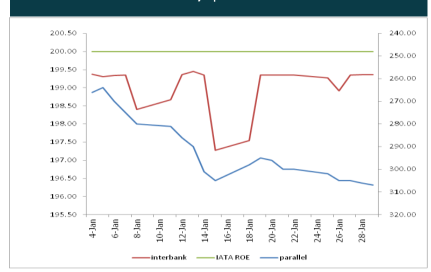
Production- Slow but steady increase

Nigeria's oil production level declined by 97,000bpd to 1.79mbpd in December from 1.89mbpd in November, as reported in OPEC's monthly oil markets report. This is 18.68% below the 2015 budget benchmark of 2.2mbpd and 0.61% below Nigeria's OPEC quota of 1.8mbpd.

FOREX MARKET

Exchange rate volatility continued in January, as market panic heightened with the ban of forex sales to Bureau de Change (BDC). As at January 29th, the naira traded at N307.00/$ at the parallel market, a 16.29% depreciation from N264.00/$ as at 31st December. While depreciating marginally at the Interbank Foreign Exchange Market (IFEM), by 0.01% to N199.36/$ at the Interbank Foreign Exchange Market (IFEM) on January 29th compared to N199.35/$ at 31st December. The IATA rate of exchange remained flat at N200/$ during the same period under review.

Chart 5: Forex N/$



Source: CBN, FDC Research

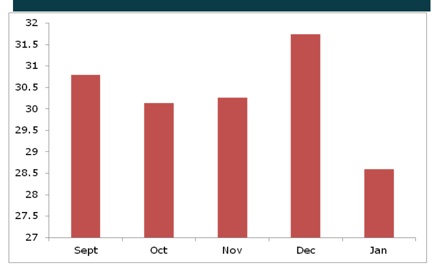
Outlook

The CBN maintained its stance on its foreign exchange market policy at its last Monetary Policy Meeting (MPC) held in January. Following President Buhari's comment and opinion on devaluation in Kenya, it is unlikely that the monetary authorities will adjust the exchange rate in the near term. In addition, the CBN initiated additional stringent policies by banning the sale of forex to BDC's with the option of sourcing forex from autonomous sources. As a result, the pressure on the naira is expected to persist at the parallel market, as depleting reserves, stringent forex policies and macroeconomic headwinds weigh on the market.

EXTERNAL RESERVES

Nigeria's external reserves depleted by 3.03% ($880m) to $28.19bn on January 29th, 2016. Year to date, the reserves level has declined by 2.72% ($790m). There has been a steady decline in foreign portfolio funds coupled with lower oil prices, which has impacted negatively on the level of external buffers. The external reserves level is 18.31% below 2015's peak of $34.51bn and 7.54% below 2015's average of $30.49bn. The level of import and payments cover is down to 4.57months from 4.72 months as at December 31st. Net external reserves level is estimated at $22.69bn, after deducting forward commitments and arrears due under letters of credit. This will bring the net reserves of import and payment cover to 3.67 months.

Chart 6: External Reserves ($bn)



Source: CBN, FDC Research

Outlook

Currency pressures are likely to intensify as CBN adopts more stringent policies to manage demand of forex. Slowing liquidity within the money market will dampen demand for forex. However, refusal to adjust the currency signals opportunities for speculative attack and round tripping. The spread between the official and parallel market is expected to widen further pending a reversal in the currency exchange narrative.

LAGOS BUSINESS SCHOOL
PAN-ATLANTIC UNIVERSITY

Executive Education

2016 OPEN SEMINARS
(February to July)

ACCOUNTING, FINANCE & ECONOMICS

Accounting & Finance for Non-Finance Executives	May 16 - 20
Financial Modeling	July 18 - 22

GENERAL MANAGEMENT

Managing Compliance and Legal Risk	May 23 - 25
Stepping up to Management	June 28 - 29
Managing People for Strategic Advantage	July 4 - 6

MARKETING AND SALES MANAGEMENT

Digital Marketing	April 11 - 13
Outstanding Customer Relationship	May 3 - 4
Essentials of Sales and Marketing	July 4 - 6
Strategic Account Management	July 26 - 28

OPERATIONS & MANAGEMENT INFORMATION SYSTEMS

Smart Business Decisions: The power of data analysis	April 18 - 22
Strategic Procurement/Contract Management	May 3 - 5
Developing Analytical Competencies for Managing Operations	June 20 - 24

PERSONAL LEADERSHIP & HUMAN RESOURCES MANAGEMENT

Building and Leading the 21st Century Team	March 21-23
Negotiation Skills & Tools	April 26 - 28
Leading with Cultural Intelligence	May 3 - 4
Mastering Human Resource Management	June 20 - 24
Improving your Personal Effectiveness	June 28 - 29
Legal Issues in HRM	June 28 - 30
Advanced HR Management	July 22 – Aug 26

STRATEGY, INNOVATION & GOVERNANCE

Sustainability Workshop for NGOs	February 23 - 24
Sustainability Reporting	March 21 - 22
Mastering Competitive Strategy and Blue Ocean Strategy	May 9 - 13
Leading a Sustainable Business	May 16 - 17 (Lagos) June 15 - 17 (Edinburgh)
Driving Strategic Innovation and Business Development	July 4 - 6

GENERAL INFO

PROGRAMME VENUE:
Km 22, Lekki-Epe Expressway, Ajah, Lagos

TIME:
9.00 a.m. - 5.00 p.m.

PRIOR REGISTRATION is mandatory to secure a place on the seminar.

RESERVATIONS / ADDITIONAL INFORMATION
Ope Oteri
0708 007 0553 / 0802 478 3267
ooteri@lbs.edu.ng

Discounts (only one category applicable)

10% off	For 5 or more nominees from the same company Per nominee on Corporate Partner Programme For individuals who pay at least 6weeks ahead of scheduled seminar
15% off	Financial members of LBS alumni Association

Download detailed calendar from our website ***www.lbs.edu.ng***

FT FINANCIAL TIMES

Lagos Business School is ranked with the world's top business schools in open enrolment executive education (2007-2015) and custom executive education (2015). ***Financial Times, London.***

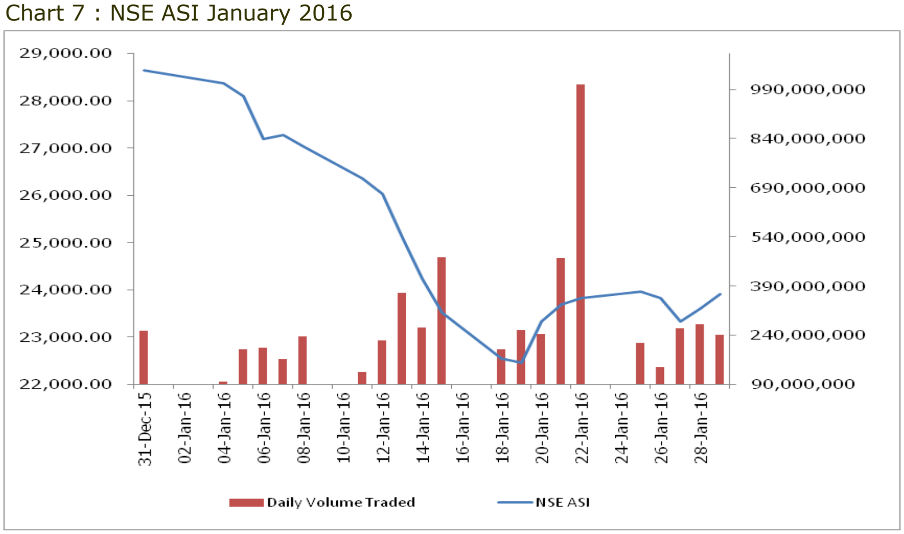
STOCK MARKET UPDATE

The Nigerian equities market retreated from gains recorded in December as NSE ASI lost 16.50% to close at 23,916.15 in the month of January, compared to the previous month's close of 28,642.25. The market lost an average of 2% daily in the first twelve days trading of the month, driven by the weak outlook about the 2015 full year corporate earnings and exchange rates volatility. The negative YTD return of the index was in line with the same period in 2015 when the market lost 14.70%. Total market capitalization, closed at N8.19trn, having lost N1.63trn during the review period.

The liquidity weighted SFNG Blue Chip 30 Index declined by 14.18% in the month of January compared with the 1.08% gain recorded in December 2015. The dividend yield and trailing PE ratio for the Blue-Chip 30 were 4.18% and 5.93x respectively while the 30-day volatility was 20.98%.

Activity on the bourse was negative as the 20 trading days in the period resulted in just 7 days of gains against 13 days of losses. Market volatility for the month was quite high as the daily changes on the ASI ranged between -4.10% and 3.91%.

Chart 7 : NSE ASI January 2016



Source : NSE, FDC Research

Chart 8 : Scott Free Nigeria (SFNG) Blue-Chip 30 (BC30) Index

Source: Scott free Index

Market activity for the month remained tepid, as total market turnover for January was N42.05bn, 26.01% lower than the N56.83bn reported in the previous month. The average daily turnover for the period also declined by 26.01% to N2.10bn from December's daily average of N2.84bn; it was also 45.59% lower than, the daily average of N3.86bn for 2015.

Market breadth was negative at 0.33x in the review period as 20 stocks advanced against 60 stocks that declined while 110 stocks remained unchanged. The best performing stocks include LEARNAFRICA 21.13%, AGLEVENT 11.29%, VONO 11.11%, CADBURY 10.79% and TIGERBRANDS 10.62%.

TOP 5 GAINERS				
Company	**Jan-16**	**Dec-15**	**% Change**	**Absolute Change**
LEARN AFRICA PLC.	0.86	0.71	21.13%	0.15
A.G. LEVENTIS NIGERIA PLC.	0.69	0.62	11.29%	0.07
VONO PRODUCTS PLC.	0.90	0.81	11.11%	0.09
CADBURY NIGERIA PLC.	19.00	17.15	10.79%	1.85
TIGER BRANDED CONSUMER GOODS PLC	1.25	1.13	10.62%	0.12

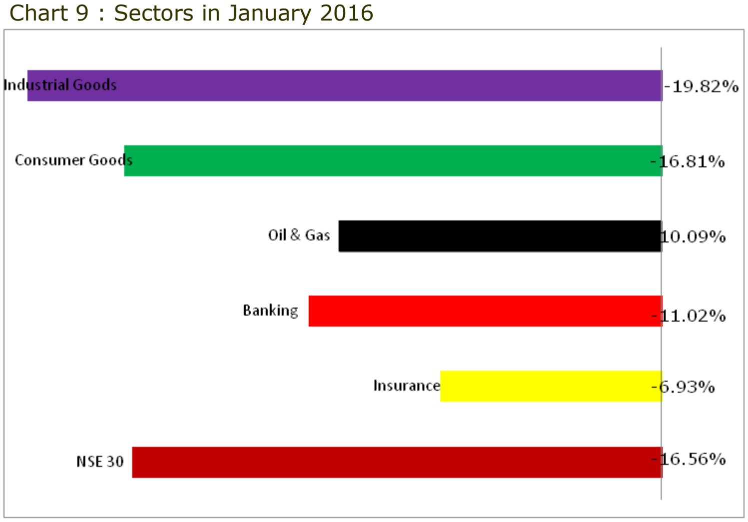
Top price losers for the month were FCMB (42.01%), UNITYBNK (33.04%), OANDO (32.20%), HONYFLOUR (28.78%) and SKYE (26.58%).

TOP 5 LOSERS				
Company	**Jan-16**	**Dec-15**	**% Change**	**Absolute Change**
FCMB GROUP PLC	0.98	1.69	-42.01%	-0.71
UNITY BANK PLC	0.75	1.12	-33.04%	-0.37
OANDO PLC	4.00	5.90	-32.20%	-1.90
HONEYWELL FLOUR MILL PLC	1.46	2.05	-28.78%	-0.59
SKYE BANK PLC	1.16	1.58	-26.58%	-0.42

5 Most Capitalized Stocks			
Company	**Jan-16**	**Dec-15**	**% Change**
GUARANTY TRUST BANK PLC	16.79	18.18	-7.65%
ZENITH BANK PLC	12.61	14.05	-10.25%
NESTLE NIGERIA PLC	739.99	860.00	-13.95%
DANGOTE CEMENT PLC	128.91	170.00	-24.17%
NIGERIAN BREWERIES PLC	100.01	136.00	-26.46%

All sectors of the ASI returned negative in the month of January, in tandem with the broad market. The Industrial Goods, which declined by 19.82%, was the worst performer for the period being reviewed. The sector's loss is hinged on the performance of industry leaders, DANGCEM (24.17%) and WAPCO (17.36%).

Chart 9 : Sectors in January 2016

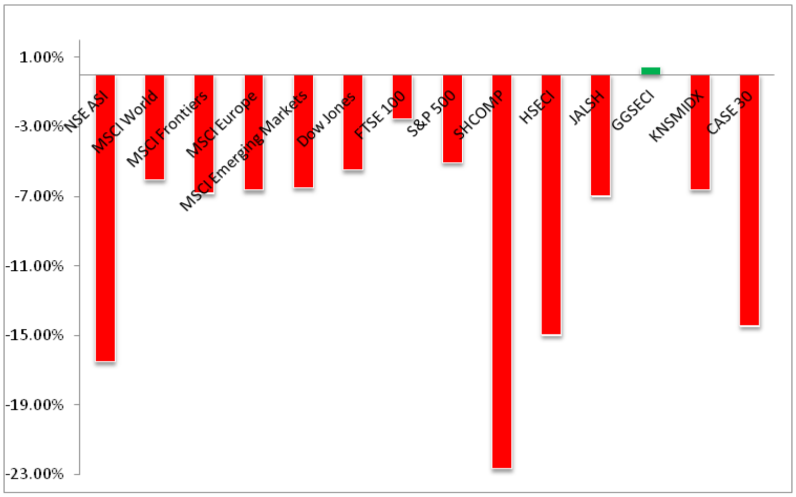


Source : NSE, FDC Research

The negative YTD performance of the Nigerian equities market has been in tandem with most global indices tracked across frontier, emerging and developed markets. The Shanghai Composite

Index (SHCOMP) was the worst performer haven lost 22.65% YTD. In Africa, the Ghana Stock Exchange Composite Index (GGSECI) was the lone gainer, advancing by a marginal 0.46%; to emerge the only index to record positive YTD performance of the major SSA indices being tracked. The Johannesburg All Share Index (JALSH), Nairobi Securities Exchange 20 Share Index (KNSMIDX) and Egyptian EGX30 Price Return Index (CASE) trended southwards in tandem with the NSE ASI year-to-date.

Chart 10 : Global Indices January 2016



Source : Bloomberg, MSCI, FDC Research

Monthly FPI transactions at the nation's bourse decreased to N51.35bn in December 2015 from N72.60bn at the end of November 2015; representing a 29.27% decline. Domestic transactions increased from 43.19% to 53.55% while FPI transactions declined from 56.81% to 43.19% over the same period. Foreign portfolio investors' inflows accounted for 15.41% of total transactions while the outflows accounted for 31.03% of the total transactions in December 2015. FPI outflows outpaced inflows, consistent with the same period in 2014. Overall, there was a 51.16% decline in total transactions in comparison to the same period in 2014.

OUTLOOK

We expected Nigerian equities market to remain bearish as investor react to the macroeconomic headwinds and uncertainty about the exchange rate outlook. Foreign portfolio investors are likely to continue to stay on the side lines pending when appropriate adjustments are made on the exchange rate. However, if impressive corporate earnings are released during the month, it may provide some relief.

CORPORATE FOCUS - DIAMOND BANK PLC

Sector: Banking **Ticker Symbols:** NSE:DIAMOND
Bloomberg: DIAMONDB:NL **Reuters:** DIAMONB:LG
FT: DIAMOND:LAG

Shares Outstanding: 323.16 bn **TP Upside:** 10.3%
Target Price: N2.12 **Market Cap:** N41.225bn

2014 Annual Dividend: N0.1
2014 Annual Dividend Yield: 5.59% **Price:** N1.9

DIAMOND BANK PLC: ***Tough economic and regulatory environment a drag on profitability***

Analysts Recommendation: HOLD

Recommendation Period: 365 days

ANALYSTS NOTE

Diamond Bank Plc (DB) financial result for Q3'15 shows improvement compared to Q3'14. Gross earnings in Q3'15 (N122.69bn) grew by 2.21% compared Y-o-Y. Customer's deposit declined from N1.493trn in Q3'14 to N1.266trn in Q3'15. Net interest income in Q3'15 grew by 3.19% to N85.2bn, compared to Q3'14, while its interest expense remained flat at N37.48bn in Q3'15 Y-o-Y.

Cost of funds marginally declined to 3.3% in Q3'15, relative to FY'14 which was 3.4%. The net interest margin (NIM) fell from 8% in FY'14 to 7.5% in Q3'15 which gives cause for concern. Its operating expenses stood at N74.37bn for Q3'15, up 4.1% compared to Q3'14; the increase was due to increased alternative banking channels and staff. Profit after tax (PAT) showed a significant decline by 27.6% to N18.59bn in Q3'15; can be attributed to a higher impairment charge. This significant impairment charge signifies the challenging economic and business environment of the banking industry. The bank's non-performing loans (NPL) ratio improved to 4.7% Q3'15, relative to 5.1% Q3'14.

In addition, regulatory policy by Central Bank of Nigeria (CBN) to increase general provisioning on non-performing loans to 2% from 1% alongside the impact of possible devaluation to negatively affected banks'. With the current market price of N1.79 and our estimate of N2.12 we place a HOLD recommendation on the stock, considering the upside potential to be limited.

PROFILE

Diamond Bank was incorporated in December 20, 1990 as a private limited company and in May 2005, it was listed on the Nigerian Stock Exchange. Diamond Bank's Global Depositary Receipts (GDR) is quoted on the Professional Securities Market of the London Stock Exchange. Its key shareholders include Carlyle Group Nigeria, a private equity fund and the International Finance Corporation (IFC), which is an arm of the World Bank.

The Bank operates three subsidiaries: Diamond Bank S.A. (97.07%), Diamond Pension Fund Custodian Limited (100%), and Diamond Bank UK Plc (100%). The indirectly wholly owned subsidiaries (via Diamond Bank S.A.) are Diamond Bank Togo, Diamond Bank Senegal, and Diamond Bank Cote d'Ivoire.

The bank is one of the leading banks in Nigeria with assets close to N1.93 trillion and more than 266 branches across the country. Its business units includes Retail, Corporate and MSME banking. The bank collaborates with the following financial institutions to provide their clients with value-adding solutions; Citibank, HSBC Bank, ANZ Banking Group, ING BHF Bank AG, Standard Chartered Bank, Belgolaise Bank S.A, Deutsche Bank, Commerzbank and Nordea Bank Plc.

MANAGEMENT

Within the course of two years, a major management team re-shuffling was observed. This saw the appointment of Mr. Uzoma Dozie as the Chief Executive Officer and Group Managing Director of Diamond Bank Plc in October 2014 alongside appointment of Dr. Chris Ogbechie as the Chairman, Chiugo Ndubisi as the acting Chief Financial Officer and Mr. Damian Dolland as non-executive director in 2015. These outstanding individuals bring along broad experience in navigating the financial service business cycle.

The company's further management team comprises of respected and experienced members who have considerable work experience in the banking space. They include: Mr. Barry Thomas, Mr. Christopher Low, Dr Olubola Adekunle Hassan, Mr. Ian Greenstreet and Chief John Edozien.

What the Bulls and Bears Say

The Bulls Say:

- The bank has significant room for profitable growth by serving Nigeria's unbanked population
- With more than 266 branches across the country and off-shores, it allows the bank offer its diverse products to a wide spectrum of customers.
- With the new government's 2016 budget of pro-infrastructure policies, the loan that accounts for approximately 29% of Diamond Bank's loan books should come back into the black.
- The bank's technologically driven strategy *mobile and internet banking* and scale advantage will help reduce costs due to the right mix of physical footprint alongside deployment of technologies.
- Devaluation of the Nigerian Naira directly affects our fair value estimate though not significantly. For example, a 10% decline in the exchange rate will result in a 0.3% fall in the capital adequacy ratio (CAR) without any deterioration in the bank's fundamentals.

The Bears Say:

- Regulatory changes in the banking sector continue to cast a shadow on the sustainability of returns at Diamond Bank.
- High exposure to power and infrastructure sectors means that loan growth can be volatile given high variability in infrastructure spending and commodity prices
- Given the prevailing macroeconomic environment, Diamond bank may face tougher competition

INVESTMENT THESIS

The banking sector is faced with sweeping changes in technology, regulations, and competition that are shaping the sector. These changes are helping meet customers' needs with less consequential risk. The interconnectivity of nations has seen Nigeria's macroeconomic risk heightened due to non-diversification of the economy from oil. The resulting effect of a low oil price is the slowing GDP growth of 2.84% in Q3'15, currency pressure, inflationary pressure among others.

DIAMOND BANK PLC VALUATION USING DDM

Our intrinsic value for Diamond Bank Plc was arrived at by using a Discounted Dividend Model (DDM) valuation method. Key assumptions include:

- The DDM valuation method is based on a three (3) year forecasted financial statement.
- A cost of equity of 20.9% (capital asset pricing model), beta of 1.77[9], risk free rate of 12.03% (the rate for a 10-year FGN bond maturing in 2025), and a market risk premium of 5%.
- Valuation took into consideration near term outlook such as the company's growth and profitability, and the prevailing

[9] Financial Times data

macroeconomic conditions, we forecast a three-year earnings per shares (EPS) CAGR of 9.13%.

- The target price of Diamond Bank Plc is N2.12, which is at 10.3% discount to the current price of N1.9 as at January 14, 2016. As such, we recommend a HOLD on the stock for a period of 12 months.

RISK

Macroeconomic Risk:

The macroeconomic environment is intricately linked to the business cycle of companies, thus; Diamond is not insulated from the prevailing macroeconomic conditions. With the abrupt fall in commodity price, Nigeria's fiscal earnings have dropped significantly with consequential effect on the broad economy. Creeping inflation and, slowing GDP growth rate among others have seen policy makers and regulatory authorities react in a swift manner to mitigate the effect. These actions have the potential to affect the bank's asset quality.

Operational Risk:

The CBN's Financial Stability Report 2015 divulges the banking sector recorded of fraud involving the sum of N11.98bn though with less cases (in total 5,917 cases). This highlights the banking space is exposed to fraud and forgeries. However, improved policy standards, 'BVN', and a control framework are being embarked on to mitigate operational risk facing the sector.

Credit/Default Risk:

The bank has a 29% exposure to the oil and gas sector. The sustained low crude oil price, has heightened the default risk. Already most of the loans and advances have been restructured to facilitate debt and interest repayment. With the low crude oil price, most Oil & Gas EP companies are trying to stay afloat and this has the potential to increase the bank's loan loss provisioning. Also, the bank's ability to repay $200mn Eurobond obligation is questionable given the present macroeconomic environment. Risk management procedure and recovery strategy deployed will help mitigate the risk.

Regulatory Risk:

One of the sector's trend is the stringent regulatory authority's policy, law, guidelines and enforcement though taken as a proactive step to negate likely spillover effect due to bank's risk exposure to other industries. These regulatory actions and policies such as removal of the commission of turnover (COT), stamp duty charges of N50, and FX restriction have all called to question the bank's topline and bottom-line sustainability. Notwithstanding, bank's engagement with regulators will help mitigate the turbulence anticipated.

Appendix

Diamond Bank PLC (DIAMONDB NL)							
In Millions of NGN except Per Share 12 Months Ending	FY 2011 12/31/2011	FY 2012 12/31/2012	FY 2013 12/31/2013	FY 2014 12/31/2014	FY 2015E 12/31/2015	FY 2016E 12/31/2015	FY 2017E 12/31/2015
Interest & inv't income	83,869.20	112,633.20	145,744.40	161,129.60	162,740.90	157,101.40	173,597.00
Interest payable <exp>	12,502.50	23,030.40	38,500.20	51,553.40	49,903.70	48,905.70	52,947.10
Net Interest Income	71,366.60	89,602.80	107,244.20	109,576.20	112,837.20	108,195.70	120649.9
Trading Account Profit	2,738.40	-2,541.10	3,768.40	8,696.90	4,131.00	3,945.10	4,043.80
Commissions & Fees Earned	19,361.50	26,496.70	29,803.00	36,589.70	32,930.70	33,260.00	34,257.80
Other Operating Income	804.7	813.4	798.3	1,985.90	1,290.80	1,097.20	1,206.90
Net Revenue	**94,271.30**	**114,371.80**	**141,613.80**	**148,151.80**	**151,189.80**	**146,498.10**	**160,158.50**
Provisions for Loan Losses	55,408.70	17,028.30	23,296.70	26,371.10	30,238.00	29,299.60	26,105.80
Net Revenue After Provisions	**38,862.60**	**97,343.50**	**118,317.10**	**121,780.70**	**120,951.80**	**117,198.50**	**134,052.60**
Non-Interest Expense	56,822.40	69,859.70	86,232.00	102,376.40	96,761.50	99,618.70	113,944.70
Operating profit (loss)	**-17,959.70**	**27,483.80**	**32,085.10**	**28,101.20**	**24,190.40**	**17,579.80**	**20,107.90**
Net Non-Operating Losses (Gains)	5.2	2.3	5.1	0	0	0	0
Pretax Income	**-17,964.90**	**27,481.50**	**32,080.00**	**28,101.20**	**24,190.40**	**17,579.80**	**20,107.90**
Tax on profit (loss)	-4,023.90	5,373.50	3,535.50	2,616.00	3,503.70	2,637.00	3,116.70
Income Before XO Items	**-13,941.00**	**22,108.10**	**28,544.50**	**25,485.20**	**20,686.70**	**14,942.80**	**16,991.20**
Minority Interests	6.3	-33.3	-31.3	76.5	38.3	19.1	9.6
Net profit (loss)	**-13,730.10**	**22,141.40**	**28,575.80**	**25,408.70**	**20,724.90**	**14,961.90**	**17,000.70**
Net Inc Avail to Common Shareholders	**-13,730.10**	**22,141.40**	**28,575.80**	**25,408.70**	**20,724.90**	**14,961.90**	**17,000.70**

☎: 7739831, 7798998, 2715414; Email: fdc@hyperia.com; Website: www.fdcng.com

Diamond Bank PLC (DIAMONDB NL)							
In Millions of NGN except Per Share 12 Months Ending	FY 2011 12/31/2011	FY 2012 12/31/2012	FY 2013 12/31/2013	FY 2014 12/31/2014	FY 2015E 12/31/2015	FY 2016E 12/31/2015	FY 2017E 12/31/2015
Assets							
Cash & Near Cash Items	55,784.10	132,196.10	228,322.10	301,393.10	346,602.00	388,194.30	427,013.70
Interbanking Assets	90,648.00	139,803.30	129,362.30	296,098.60	193,766.90	201,905.10	210,990.80
Short-Term Investments	94,032.30	100,712.80	14,520.30	13,793.70	37,053.20	37,794.30	38,739.10
Net Loans	388,136.50	585,200.20	689,168.30	791,094.70	810,872.00	831,143.80	851,922.40
Long-Term Investments	96,652.80	145,065.20	368,619.60	435,919.90	398,866.70	408,838.40	424,374.20
Net Fixed Assets	39,664.50	44,980.30	49,827.30	55,062.10	61,172.80	67,290.10	73,346.20
Other Assets	31,313.60	30,145.90	39,036.40	39,761.30	59,642.00	60,834.90	63,876.60
Total Assets	**796,231.80**	**1,178,103.80**	**1,518,856.40**	**1,933,123.40**	**1,907,975.70**	**1,996,000.80**	**2,090,263.10**
Liabilities & Shareholders' Equity							
Customer Deposits	603,003.20	910,234.40	1,206,044.00	1,493,081.20	1,433,358.00	1,462,025.10	1,505,885.90
ST Borrowings & Repos	33,825.40	36,110.90	54,579.50	68,760.40	87,944.60	114,328.00	144,624.90
Other Short-Term Liabilities	1,346.90	15,221.10	17,125.20	12,608.20	12,605.70	12,731.80	13,050.10
Long-Term Borrowings	42,035.30	64,430.50	68,395.10	106,495.80	110,755.60	118,508.50	125,619.00
Other Long-Term Liabilities	30,040.00	43,251.00	33,859.00	43,153.00	48,503.90	56,507.10	67,938.40
Total Liabilities	**710,250.80**	**1,069,248.00**	**1,380,002.70**	**1,724,098.60**	**1,693,167.80**	**1,764,100.40**	**1,857,118.30**
Total Equity	**85,981.00**	**108,855.70**	**138,853.70**	**209,024.80**	**214,807.90**	**231,900.40**	**233,144.80**
Total Liabilities & Equity	**796,231.80**	**1,178,103.80**	**1,518,856.40**	**1,933,123.40**	**1,907,975.70**	**1,996,000.80**	**2,090,263.10**