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Managing Equity Investments during Market Downturns

In this time of economic slowdown investors may be asking themselves if they have the appetite to stay in the market. Periods of recession or economic downturn are rife with uncertainty, dampened appetite for investments and heightened risk. The natural response in such periods may be to delay investing until conditions improve. In extreme cases, investors may pull out of the markets all together.[1]

The financial crisis/global recession in 2008 left a bad taste in the mouth of investors. Some vowed never to return to the stock market while others reduced their participation to the barest minimum. The Nigerian stock market was not exempt. Between 2008 and 2009, investors witnessed significant erosion in the value of their investments as the market lost N7.24trn from a high of N12.64trn.[2] This saw reduced participation in the stock market for both foreign and domestic investors.

As the current economic slowdown shows its ugly head, investors will be less likely to make the same mistakes as those made in 2008/2009. As the old saying goes: once bitten twice shy. Investors are likely to remain on the sidelines until there is some semblance of recovery. While accepting that this approach (which is purely risk averse) is understandable, there are approaches to investing that can be used when transacting in the stock market especially during downturns. Most importantly, investors must re-

[1] Investopedia, 2009, Top 6 Recession Investing Myths

[2] www.nse.com.ng

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spond strategically rather than react to market developments in periods of slowdown. With a bit of pro-activity and flexibility, investors can still participate in the market, despite the economic downturn.

Here are a few ways on how to stay invested:

- Take advantage of lower stock prices to increase their holdings especially if they have a long term outlook. By purchasing additional stocks, investors also reduce their average unit cost of purchase. Another good strategy is identifying oversold stocks to purchase (i.e buying into a stock that has seen a lot of selling and is ripe for a turnaround).
- Invest in dividend paying companies with consistent paying policy or defensive stocks with good dividend history.
- Manage losses – Markets exaggerate themselves in the direction of losses. Therefore losses have to be minimized. This can be done by setting and adhering to price limits. Stop loss orders, usually executed by brokers, are designed to limit investors' loss on a position in a security. With a stop loss order, a market order to sell is triggered when the stock trades below a certain price and it will be sold at the next available price.
- Be ambivalent about bear markets – adopt the right mental approach, knowing there are opportunities also in Bear markets.
- Diversify across asset classes and investment types to reduce risk. Having a percentage of your portfolio spread amongst stocks, bonds, cash and alternative assets such as real estate assets, is the core of diversification. A proper asset allocation strategy will allow you avoid the potentially negative effects resulting from placing all your eggs in one basket.
- Invest in assets that help preserve capital.
- Avoid increasing your borrowing especially to invest in the stock market. This is clearly not a time to increase leverage.
- Consider Inverse ETFs. Investing in ETFs is similar to using a combination of advanced investment strategies to profit from declining prices. Even though these are instruments which are

not available in the Nigerian investment space, they are readily available in developed markets.

- Play safe. Playing safe means putting a larger portion of your portfolio in money market securities such as fixed deposits, treasury bills and other instruments with shorter maturities and acceptable yields.[3]

Investment strategies have to be dynamic. Different strategies should be adopted in periods of boom and bust. The best advice one can give during a recession is to take the time to revisit long-term goals, and adjust overall asset allocation to protect assets.

It is important to note that inspite of all the strategies out there, nothing is entirely foolproof. It is expected that investors proceed with caution and also seek the services of professionals who would offer guidance.

[3] www.ruleoneinvesting.com

Economic Investments from a Different Lens: The Advantages of Investing in Trust

The current economic slump plaguing Nigeria has led to a debate: what measures Nigeria should have taken to better equip the economy against these negative shocks? Economists have long come up with theories to help facilitate sustainable long run growth. There is the neoclassical model of growth,[4] which stresses physical capital investment through savings (as savings are a medium for investment funding), a reduction in population growth, and technological progress. Then there is the endogenous growth model, which stresses accumulating human capital - a knowledgeable and productive workforce - through education and grants for research and development.[5] The expectation is this investment leads to innovation, which moves the economy forward; as a few entities gain knowledge in a particular sector, all others in the sector are able to partake in this process through knowledge transfer and imitation.[6] These theories have helped shape policies in many countries. However, they come with their own drawbacks. These drawbacks include the inability of these models to fully explain growth movements in country samples. The neoclassical model indirectly argues that long-run growth movements are outside the control of Nigerian policymakers and are hence subject to external factors, these factors being elements that drive technological change. Endogenous growth models do not acknowledge the catch-up factor that is observed in the world today where less developed countries like China have higher growth rates than that of more developed countries like the US.

For these reasons there is cause to look at another method through which sustainable economic growth can ensue- social capital.[7] Social capital can best be described as the civic norms

[4] Solow, Robert. 1956. A Contribution to the Theory of Economic Growth. *The Quarterly Journal of Economics.* Vol. 70, No. 1, pp. 65-94

[5] Endogenous growth model pioneers include Kenneth Arrow (1962), Hirofumi Uzawa (1965), Paul Romer (1986), Robert Lucas (1988).

[6] This is also known as cluster or spatial economies, where as a result of the knowledgeable few being located in an area, individuals are able to learn from each other and innovation becomes the norm. An example of this is Silicon Valley in the US.

[7] Alejandro Portes (2000) argues "the concept of social capital is arguably one of the most successful 'exports' from sociology to other social sciences and to public discourse during the last two decades".

and engagement as well as the trust culture, which bring about both economic and political progress.[8] In many empirical studies, trust is often used as the major proxy for social capital. Political scientist Francis Fukuyama argues that:

"….. one of the most important lessons we can learn from an examination of economic life is that a nation's well-being, as well as its ability to compete, is conditioned by a single, pervasive cultural characteristic: the level of trust inherent in the society."[9]

Trust can be defined as the belief that others will not deliberately or knowingly do us harm if they can avoid it, and will look after our interests, if it is possible.[10] Putnam describes trust, as well as other forms of social capital, as a means to solve the dilemmas of collective action and cooperation, which is necessary for economic and political progress. He argues that the reason why nations are seemingly backward is not due to ignorance or irrationality, as to the benefit of cooperation facilitating economic growth, but rather due to a lack of trust; individual entities are afraid that once they stake their investments as a contribution to collective action, other parties involved would default on responsibilities.[11] Fostering social capital in an economy has the effect of reducing transaction costs such as cost of monitoring, which impede on the ability for businesses to take shape and thrive, which in turn feeds into the macro economy. Robert Putnam argues that trust, which is a form of contract, begets collective action, which helps the society progress politically, economically, and socially.[12]

Italy, in the 1950's, was a natural experiment highlighting the benefits of trust. In northern Italy, where there was more trust, Putnam was able to establish a correlation between collective action and economic progress. Hence, there was more development and greater income was earned when compared to southern Italy, Merzzogiorno,

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[8] Putnam, R.D. (1993), Making Democracy Work: Civic Tradition In Modern Italy, Princeton Press Paperback Edition, USA.

[9] Fukuyama, F. (1996), Trust: The Social Virtues And The Creation Of Prosperity, Penguin Groups, Great Britain. Page 7.

[10] Dehley, J. and Newton, K. (2005). "Predicting Cross National Levels Of Social Trust: Global Pattern Or Nordic Expectionalism". European Sociological Review. Vol. 21, Pp. 311-327.

[11] Putnam, R.D. (1993), Making Democracy Work: Civic Tradition In Modern Italy, Princeton Press Paperback Edition, USA.

[12] At the time of this study the south was more prosperous although in modern times the north has come up in terms of income earnings.

which had very little trust to guide public and private relationships. This was due to the kind of institutions imbibed in the region. Fractionalization in the form of trade restrictions, as well as a surge in mafia and brigandage units wrecking havoc through violence and corruption, fed into the way the citizens of Merzzogiorno formed their trust expectations.

Just as was the case in southern Italy, Nigeria has a significant trust deficit driven by a highly fractured ethno-linguistic population profile. In a 1997 cross-country study of market economies, Knack and Keefer recorded an extremely low percentage of respondents who said, "most people can be trusted" in Nigeria.[13] This means roughly 78% of the population is distrustful. Now, given Nigeria's present condition following a decline in oil prices (and hence oil revenue), a weakened naira, and a decline in foreign exchange reserves, policy makers are looking for ways to encourage collective action and kick start the economy with increased business activities. However, in a society where there is a lack of trust from the individual unit to the government and institutional units, this is close to impossible.

Given the various positives that trust introduces to economies, such as: reductions in transaction costs, innovation, physical and human capital accumulation, and higher returns to both physical and human capital, policy in Nigeria should be constructed in such a way that a trusting culture is developed.[14] Hence, in the sphere of governance, state and federal governments should strive to be increasingly transparent with their policies as well as communicate effectively what these policies entail to the masses. This would foster a trusting relationship between government and the citizens of Nigeria. More programs like the National Youth Service Corps (NYSC), which ultimately strive to break down barriers of culture and religion, in order to foster tolerance amongst the youths, should also be encouraged as this ultimately builds trust.

13 Knack, S. And Keefer, P. (1997), "Does Social Capital Have A Payoff? A Cross-Country Investigation". Quarterly Journal Of Economics. Vol.112, Pp.1251–1288

14 K. Nielsen, "Social Capital and Innovation Policy" <http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.195.5121&rep=rep1&type=pdf>

Investing in outreach programs to enable indigenes of Nigeria to better understand one another could be another step towards understanding and tolerance. Encouraging a significant portion of the ethnic groups in Nigeria to engage in and take certain seats in government and public sector institutions would help pacify disdain towards certain tribes that consistently hold power, thereby fostering trust in government and institutions. The current government is more focused on its anti-corruption war and hence can be rather myopic when it comes to certain theories and policies. Taking social capital accumulation as a matter of precedence is unlikely to occur in the short term or even the medium term but it would be well worth the investment.

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5. Fully equipped play area for children

Global Perspective – *Culled from the Economist*

Smuggling in Nigeria

Blurred lines

The government's protectionist policies are keeping the bootleggers in business

There is a clamour down the tiny alleyways of Kano's central market, in northern Nigeria, as vendors thrust fabrics at passers-by, promising the best colour, quality and price. Amid the racket, Alhaji Zakari sits cross-legged on his countertop, surrounded by materials marked "Made in Côte d'Ivoire". "They're not", he says with a degree of honesty which can do little good for sales. "It's imitation from China."

Nigeria is awash with contraband. Chatham House, a British think-tank, reckons that at least 70% of trade between Africa's biggest economy and its neighbours goes unrecorded. In 2010, the World Bank estimated that $2 billion worth of textiles like Mr Zakari's are squirreled into Nigeria every year.

One bootlegger supplying the latter is Adamu Muhammad, or so he gives his name. Like many others in the north, his syndicate brings goods in through Cotonou, Benin's main port and commercial capital, then through Niger, and across Nigeria's border. For a decade, convoys of up to 50 of the syndicate's vehicles have rattled into Kano without obstruction, because bigwigs in the capital were paid to let them pass. A lucrative lorry-load may command a fee of up to 1m naira ($5,000 at official rates), Mr Muhammad says. In return, "Everyone is settled—from Niger to Kano."

Sadly for his crew, that party is now over. Almost a year ago Nigeria acquired a stringent new president, Muhammadu Buhari, who has vowed to crack down on corruption. He put trusted counterparts at the top of misbehaving agencies such as the customs department, so it is now harder to get the sign-off for illegal deliveries. It seems to be working: Mr Muhammad says his friends must wait until the process can be "facilitated" again.

Mr Buhari has affected cross-border business in other ways, too. Nigeria's economy, dependent on oil (the price of which has slumped since 2014) is in dire straits. In a bid to conserve foreign exchange, Mr Buhari has imposed harsh restrictions on imports of goods that he reckons could be made at home. As a result, the value of the dollar has soared on the black market, making it increasingly expensive to buy from abroad. In Benin, huge car dealerships used to do a roaring trade with Nigerians who smuggled vehicles through the bush. They are now eerily quiet. A peeved merchant of second-hand tyres says he is doing "zero business".

Another part of the reason that goods are secreted into Nigeria is that shipping to Lagos is slow and bureaucratic. Customs officials ask businesses to produce 13 documents when they bring a shipment in, and nine on the way out. Corruption is rampant, and tariffs are high. Import bans on items including rice and carpets are supposed to protect local businesses, but instead push trade underground and make rich the cronies who win waivers. It is no coincidence that women cross into Nigeria carrying rice on their heads, or that Mr Muhammad also specialized in deliveries of cooking oil and pasta, the import of which is supposedly banned.

This hurts Nigeria's economy (in 2010 the World Bank estimated annual revenue losses from smuggling of $200m). Despite the efforts to protect them only a handful of the 175 companies producing local fabric in the mid-1980s survive today.

The World Bank says that removing import bans would lift 4m Nigerians out of poverty. Unfortunately, Mr Buhari thinks that barriers will help shore up the currency and stimulate domestic production. Under his watch, foreign exchange has been banned for imports of 41 items, including glass and wheelbarrows.

History shows this will not work. At Benin's Seme border post, an immigration official watches a motorbike laden with rice whizz past and declares, with a smile: "Smuggling is easy."

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Issues and Challenges of Governance in Nigeria

by

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A lecture delivered at the launch of the Endowment Fund for instituting the Oba Sikiru Adetona Professorial Chair in Governance in the Department of Political Science at the Olabisi Onabanjo University, Ago-Iwoye, Ogun State.

Highlights

Issues and Challenges of Governance: (a) the Federal Level

The 1962-1966 political imbroglio in the country led to the collapse of the First Republic and the end of the parliamentary system of government which the country had adopted from the experience of its colonial master. The military government that took over the administration of the country noted that, apart from restructuring the country from four regions to twelve states, there was need to design a more robust Constitution that takes cognizance of Nigeria's peculiarities especially its multi-ethnic character, its religious differences, the different levels of socio-economic and socio-political development of the various nationalities that make up the country. There was need for a system in which all these nationalities and ethnic groups could have a say in the selection of their Head of State and of Government of the Nigerian Republic. It was reckoned that such a system would ensure that the Head of State/Government would strive to be sensitive to being acceptable to all parts of the country and not just his small constituency as was the case in the single-member constituency structure of the parliamentary system of government. It was also felt that there was need to minimize the importance of regional political parties in the determination of national affairs.

The 1979 Military Constitution thus chose a Presidential System of Government of the American type which it believed provided the answer to all of these national challenges. This system requires that the President is elected by the majority of the Nigerian population in their different nationalities and states. It emphasized the separation of powers as between the Executive (the President and his Ministers), the Legislature and the Judiciary. It empowered the President (the Executive) to man the different Ministries of Government with personnel brought generally from outside of the elected members in the legislature. It also empowered the President to employ in addition needed advisers and special assistants from outside the Legislature to facilitate governmental operations. The system required that policies and programmes derive essentially (but not exclusively) from the President so as to provide a focused, consistent and decisive strategy for national development and security with the Legislature having principally an oversight function to ensure transparency and accountability on the part of the Executive, apart from passing the budget for implementing the policies and programmes.

In spite of being an apparent answer to the challenges of Nigeria at the Federal level, the American-type Presidential system has many striking demerits in a country like Nigeria which is still trying to find its feet as a democratic and a developing nation. For one thing, the idea of a governance system based on the separation of powers ends up, as it were, positioning the Legislature almost as the opposition to the Executive, even when the President's party has a majority in the National Assembly. In other words, the system does not necessarily align the majority party behind the policies and programmes of its President, thus rendering party manifestoes of little importance in evaluating the post-election performance of the party in power. It thus makes for weak party control and discipline of the legislators as we've seen in the present National Assembly. It provides virtually little opportunity for serious political education of politicians by denying legislators the reward system of ministerial promotion for those showing good grasp and expertise in tackling the intricacies of particular sectors of national socio-economic life and loyalty in promoting the policies and programmes of the party whether in government or in opposition. More than this, the Presidential system is very costly especially in terms of the range of personnel appointable by the Executive (ministers, advisers, special assistants, etc.) and the need to provide separate constituency development fund to the legislators even those whose party is in power. More seriously, the Presidential system tends to foster and promote corruption in the decision (or budgetary) interface between unelected Ministers sitting on and dispensing large national resources while elected legislators are confined, as it were, simply to legislative duties and oversight functions. This, of course, is where the "awuff" mentality comes into play.

By 1979, when Nigeria was opting for the American-type Presidential System of Government, there was another Presidential System which was emerging world-wide as an alternative to either the Parliamentary System of government. Indeed, this system combines the best features of both the parliamentary and the American-type system and is often referred to as the Semi-Presidential system of government. The system admits of an Executive President elected by all of the electorate in the nation and has powers over defined areas of government such as Foreign Affairs, Defence and Security whilst having a Legislature from amongst the majority party of which a Prime Minister and Ministers are chosen, whose performance is constantly under the direct scrutiny of the Legislature. There is no Vice-President in the system and the division of functions as between the President and the Prime Minister varies from country to country. Similarly, the question of the tenure of office of a government under a Prime Minister is based on the ability to muster a majority in the legislature and can be determined by a negative vote of confidence in the National Assembly. The Legislature thus elects its own Prime Minister and Ministers but these are formally approved by the President who also has the responsibility of formally dissolving the Legislature whenever its term expires.

The Semi-Presidential system which is similar to what obtains in France and some 40 other countries has certain advantages that make it more suitable for the Nigeria political situation than the American-type Presidential system. .By preserving the system of a President elected nation-wide, the semi-presidential systems meets the challenge of the Nigerian situation. By removing the position of Vice President, it has done away with one of the causes of unnecessary tensions and conflicts in the administration of the country. By emphasizing the choice of Prime Minister and Ministers from among the elected representatives of the party in power, it enhances the process of political and policy education among politicians and removes the "awuff" temptation in the process of passing the annual appropriation bill as a surreptitious factor of corruption in governance. More than this, the capacity of political parties to choose from among their member-legislators both serving and shadow Ministers fosters greater party discipline and ensures greater loyalty, attention and commitment of party members to the implementation of the party manifesto and programmes. It also facilitates wide-ranging consultations among legislative members of the party in power and ensures their alignment behind critical policies of their government such as the withdrawal of petroleum subsidy.

The semi-presidential system also enables up-and-coming legislators to fill in positions such as advisers and special assistants and even if some of these are needed from outside the legislature, the number can be pegged down significantly. It certainly obviates the corruption that is fostered in the interface of transactions between unelected Ministers and elected legislators and, more importantly, it drastically reduces the cost of governance in the country. For Nigeria, a system that makes recurrent expenditure more than 70 per cent of the annual budget can hardly be said to be in the best interest of the need for the rapid economic development of the country. More than that, a system that has no inbuilt structure for the political education and reward for increasing competence among politicians cannot be good for a country in the early stages of democratic consolidation. Furthermore, a system that does not enhance the capacity of a government to have an executive and a legislative majority aligned in promoting the election-winning manifesto and programmes of its parties cannot foster the growth of a disciplined multi-party democracy in the country.

Issues and Challenges of Governance: (b) at the State Level

The Petroleum Act of 1969 began the process of changing the relationship between the regions and the Federal Government. Up to that time, although mining and minerals were on the exclusive Federal Legislative list, the Federal Government did not claim any exclusive rights to those resources. Indeed, as already indicated, it allowed the regions where such resources were found to keep 50 per cent of the royalties and rent whilst 30 per cent went to the distributable pool to be shared among the regions whilst only 20 per cent accrued to the Federal Government. The 1979 Constitution concretized this new relationship with the creation of a "Federation Account" into which shall be paid all revenues collected by the Government of the Federation. It went on to state that "any amount standing to the credit of the Federation Account shall be distributed among the Federal and State Governments, and the local government councils in each State , ***on such terms and in such manner as may be prescribed by the National Assembly.*** Please note the difference between the "Distributable Pool Account" to which the Regions all contributed 30 per cent of their claims from royalties and rent so as to assist in evening out development across the country and this new "Federation Account" which swallows all revenues from the States and leaves them able only to have their share as determined by a body known as the Revenue Mobilization and Allocation Fiscal Commission set up by the National Assembly.

This constitutional amendment, in a sense, not only undermined the fiscal independence of States and made their sustainable development a function of how prudent they manage their allocation from the Federation Account. It also discouraged States from striving for novel and innovative ways of raising new revenue. More than this, it made it possible for the Federal Government to begin to give away States and Local Governments on an "awuff" basis. Whilst it can be claimed that the first set of 12 states created in 1967 was exigent as a means of keeping the Federation as one, all subsequent creations of States and Local Governments cannot be justified on any other basis than that some of the agitators for those States knew someone at the highest level of the Federal Government. Most of these States were thus created without asking the fundamental question as to their long-term viability or ability to provide their citizens with needed services. Because these questions were not asked at their inception, most State governments became lay-back as far as raising the necessary resources for good governance. They would rather troop out to Abuja on a monthly basis to get their share in the monthly distribution of the Federation Account which, because it is "awuff" can easily be misappropriated to personal and other uses. The challenge of seriously seeking and exploiting innovative and more robust and enduring ways of generating resources for the good governance of their States was hardly contemplated by many State Governments. The manner in which a number of State Governors ended up in the clutch of the EFCC at the end of their term in office underscores how deleterious against good governance has been the institution and role of the Federation Account in the development of Nigeria.

But perhaps more serious is the impact of this "awuff" money on the economy not just of Nigeria as a whole but of its states. A well recognized syndrome in such circumstances is what has come to be known as "the Dutch disease". This is described as "the negative impact on an economy of anything that gives rise to a sharp inflow of foreign currency such as the discovery of large oil reserves." The currency inflows lead to currency appreciation, making the country's other products less price competitive on the export market. It also leads to higher levels of cheap imports and can lead to de-industrialization as industries, apart from resource exploitation, are moved away to cheaper locations outside the country. The syndrome has militated against most State governments paying attention to the development of the more authentic bases of their economies, revenue from which could have bolstered their overall revenue position.

As against this situation, it has been argued that Lagos State in particular has thrived economically very strongly in spite of these circumstances owing to its special location as a port city, an industrial centre and the former capital of the country. While these cannot been gainsaid, it is also true that Lagos State has been one of the few which had paid critical attention to its other basic resources in land and property administration. It was this that could allow it to resist the buffeting of the Federal Government when it refused to release to it funds due to its local governments. The positive situation in Lagos, of course, derives very much from the municipal property registration of the colonial Government which was extended to cover a large part of the State under the civilian Governorship of Chief Lateef Jakande who had embarked on the project of providing Lagos with a mono-rail and needed to indicate to prospective private investors a viable source of revenue, independent of the Federation Account.

The end of the era of the "awuff" syndrome is patent in the present situation where with the dramatic fall in the global price of petroleum a majority of "free gift" states in Nigeria have been unable to pay the salaries of their civil servants for many months, an item that should be the very first on the list of annual appropriation and expenditure. For the first time in the history of the country, voices are being raised as to the viability of many of these states. It has been suggested that the country may be well advised to use the SIX geopolitical zones as the basis for a new set of regions so as to reduce the high level of recurrent cost of governance and release needed funds for infrastructural development all over the country.

The jury, in respect of the viability of a number of the present 36 states is probably still out. Indeed, it can be argued that the first step on the future of the State structure of the country is to establish a system in which internally generated revenue of States must be adequate to cover recurrent expenditure and any subvention from the Federation Account should be to enhance infrastructural development in the State. A protocol should then be developed to enable States that cannot meet this viability criterion to be prepared to merge with a neighboring State.

Issues and Challenges of Governance: (c) at the Local Government Level

It is, however, at the local government level that the "awuff" syndrome did the greatest damage to governance and, more seriously, undermined the prospect of consolidating a virile and robust democratic culture in the country. It was Alexis de Tocqueville (1980: 54) who noted during his visit to the United States in the 19th century, that the strength of their democracy, indeed, of any democracy, is based on the institution of local governments. According to him:

"…local assemblies of citizens constitute the strength of free nations. Town-meetings are to liberty what primary schools are to science; they bring it within the people's reach, they teach men how to use and how to enjoy it. A nation may establish a system of free government, but without the spirit of municipal institutions it cannot have the spirit of liberty."

Yet, when the military decided to reform our local government system they were totally indifferent to the existing "local assemblies of citizens" or the importance of their "town meetings". Instead, in other to be able to give them "awuff" money, they created "artificial local governments" based on a demographic criterion. This sought to create local governments in Nigeria on the demographic principle that "no local government should have a population of less than 150,000 and not more than 800,000". (FRN, 1976; Adamolekun & Rowland, 1979) On this basis, the country was divided into 299 local government areas. The system paid no regard to the basic human process of settling in urban or rural areas. It merged into a single local government a number of small to medium towns with the villages around them; it broke up large cities and metropolitan areas into two, three or more local governments; it tried to carve out parts of large cities and merge them with neighboring smaller centers to form a local government where the population was less than the expected number. Mobalufon in Ijebu-Ode was thus made to be part of Odogbolu Local Government. What we had was thus a number of amorphous local governments with no inherent cohesion or social *raison d'etre.*

Not unexpectedly, as soon as the particular military government handed over to a civilian regime, the agitations for a local government system that is better aligned to the wishes and aspirations of the people became strident all over the country. Most State governments began to respond to these reasonable demands of their people. The Buhari coup of December 1983 truncated these developments as it regarded the agitations as another evidence of the social indiscipline in the country. Consequently, the country was forced back to the system of 299 local governments. But the agitations continued forcing the succeeding military government of General Babangida to increase the number first to 489 and later to 569 but without pretense to any objective criteria or rationality. Since even with this relaxation the agitation continued right up to the regime of General Sani Abacha, the latter responded to it by creating more States and local governments, this time clearly on the basis of his whims and caprices. Thus, Lagos and Kano State which, up till then had the same number of TWENTY local governments each, suddenly found that Kano State from which a new State, Jigawa State, was carved out was assigned 44 local governments and the new Jigawa State another 26 local governments whilst Lagos State remained with only 20 local governments. On this basis, the country ended up with 768 local governments excluding the area councils of the Federal Capital Territory. It is this number of local governments that entered into the 1999 Constitution of the country.

The 1999 Constitution has three main sections on Local Government apart from a Fourth Schedule which spells out their functions. Section 7(1) states: "The system of local government by democratically elected local government councils is under this Constitution guaranteed; and accordingly, the Government of every State shall subject to section 8 of this Constitution, ensure their existence under a Law which provides for the establishment, structure, composition, finance and functions of such Councils." Section 8 (5) & (6), however, virtually took away these powers of the States since it requires the National Assembly to approve these local governments so "established" by having to pass "An Act of the National Assembly …. to make consequential provisions with respect to the names and headquarters of such local government areas." Section 3(6) further shows the diminution in the powers of States to "establish" their local governments by stating that "there shall be seven hundred and sixty-eight local government areas in Nigeria…" All of this intrusion of the Federal Government into an area which is properly within the purview of the States is, of course, because of the "awuff" resources which the Federal Government provides for local governments from the Federation Account.

What has made it difficult to reform this lop-sided local government system was the fact that from General Babangida's time, the local governments were made to receive "awuff" subventions directly from the Federation Account. Thus, the more local governments a State has, the more it received from the Federation Account. To reform the local government system on an equitable and rational basis thus looked like reducing the resources accruing to those States which had enjoyed the inequity of the Sani Abacha's local government creation. There is, however, no denying the fact that the local government areas are simply subdivisions of a State. The summation of their population or territorial extent is no greater than that of the State of which they form parts. Thus, the criteria used for providing subventions to States from the Federation Account could equally be used for subventions to their local governments even when the ratio of entitlement for States and Local Governments could be different. More seriously, however, is the fact that the attempt to ignore the different settlement patterns and therefore traditional local governments in each state of the Federation has done great harm to the efficiency and effectiveness of this level of governance in the country.

Indeed, it can be said to have confused administrative effectiveness with economic efficiency. For one, it tried to obliterate the distinction between urban and rural settlements with their very different infrastructural and socio-economic requirements. Indeed, nowhere in the Constitution is there a reference to urban development in the country. Yet, one of the most important phenomena that accompany the development of any country is the rise in the level of its urbanization. This was why as Britain began to industrialize in the 19th century it had to pass the Municipal Development Act in 1835 which sought to provide for the financial and management requirements of the infrastructural needs of urban centers such as tarred roads, street lighting, storm water drainage, internal transportation and traffic system, waste disposal and other specialized needs of urban centers like reticulated water and electricity systems not required in rural settlements. Furthermore, the local government reform by ignoring rather than building on, the traditional structure of local governments in the country alienated itself from the needs of the common man and thus virtually became irrelevant to serious governance in the country.

What this indifference to historical and cultural antecedents did was to destroy the integrity of local administration; or in other words, it made citizens no longer concerned or able to influence the quality of the people who aspire to rule them. This in itself fostered the burgeoning rise of corruption at the local level. To make matters worse, the military regime insisted that those who intend to contest any election, even one as prosaic as that to a local government council, must first resign from their paid employment. The idea of teachers, lecturers and other public officers (other than civil servants) being allowed leave of absence to serve their local communities in this manner thus became no longer possible. It thus left the field to people in the private sector, most of who operate in the informal sector generally with limited education and appreciation of the importance of local governance. The idea of serving the community on the basis of being paid "sitting allowance" thus disappeared and corruption blossomed at this level of government.

One consequence of the reformed local government is simply that it undermined the access of government at this level to the robust resource of "social capital" which had in the past been responsible for development in many urban centers of the country. Social capital (Putnam, 1993) refers to resources in kind or cash which people are prepared to deploy for the development or welfare of their home communities. It is this form of capital that had been responsible for the building of many schools, churches, mosques, post offices, community banks, water and electricity supply to many communities not able to depend on or wait for governmental provenance (Honey & Okafor, 1998). The amorphous nature of the present system of local governments simply made it impossible to mobilize this type of resources although some communities still continue to access this resource on an informal basis. But generally it has not been possible to deploy a robust system of social capital to complement or enhance effort at good material and infrastructural development at the local government level.

One other deficit of the present system of local government is that it provides relatively little opportunity for the citizens or the community at large to have much say in their governance. Although the usual cliché is to assert that local government is the government nearest to the grassroots, there is little evidence that the grassroots feel any closeness to the present local governments. No local government, for instance, submits its annual budget to its local community or reports its achievements to them, except at great expense sometimes on the pages of newspapers. In truly democratic dispensation, these are the usual reasons for holding "town-hall meetings", to enable the elected officials of the town to report to the citizens of the town and receive feedback from the citizenry and directions for the future. It is at such meetings that democratic learning is nurtured and participatory democracy strengthened such that people are encouraged to learn how to put their purse where their mouth is in terms of the development they desire for their local environment. Instead of this, the present situation in Nigeria is that it is State governors that hold town hall meetings, especially during their campaign tours to a town which could thus be once or twice over a four-year period and it is always so fleeting and riotous.

This absence of a forum or a Town Hall meeting to discuss the problems of a given locality and how to resolve them has been a major reason for the inability of local governments to improve on their internally generated revenue instead of depending almost wholly on subventions from the Federation Account. It is this opportunity that traditional Town Unions and Development Associations had that enabled them to make more impact on the development of their communities. Apart from being open to all citizens of the area, membership of such a Town Hall meeting should include neighbourhood leaders, leaders of different occupational and informal sector trade associations, representatives of the local chamber of commerce, leaders of women and youth associations, religious and traditional leaders as well as representatives of non-governmental organizations within the local government area. The list should cover critical groups in the area whose advisory deliberations can easily be transformed into decisions of the council.

More than this, the failure to distinguish between urban and rural settlements had made it impossible for Nigeria to establish a mayoral system for its municipalities and denies her participation in international conferences of mayors of cities. It has also made it difficult to evolve appropriate management systems for agglomeration bigger than cities such as metropolitan authorities which oversee the transportation planning and development of expanding urbanized areas. When the Kano State Government during the first coming of Alhaji Kwankwaso attempted to establish such an authority for the orderly planning and development of the extensive urbanized Kano, the local governments protested that he was circumscribing their authority and resources.

Conclusion

I believe I have said enough to emphasize that the major issues and challenges facing governance in Nigeria at all levels is largely structural and derive from the military government wanting a federation turned upside down to align with the unified command structure of military administration. So, as we contemplate the future, it is my earnest hope that our political leaders would re-visit a number of institutions deriving from the period of military rule, especially the local government system. They should help create truly effective democratic local governments for the governance of our towns, cities and rural areas so as to empower the citizens and make them take ownership of their governance at the local level. Re-visiting our governance system at the State and Federal level should be specifically to cut down the cost of governance at those levels and make governance more efficient and effective for collective service delivery to citizens.

FOR THE FULL DOCUMENT CONTACT FDC THINK TANK.

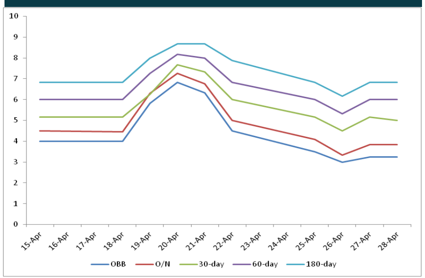
Macroeconomics Indicators

Money Market

The opening liquidity position in the money markets for the second half of April was lower than that of the first half of the month. On the 15th of April, markets opened at N351.38bn long compared to March 15th's position of N201.03bn long, hence, a 74.8% decline. On the 29th of April, markets opened N454.2bn long compared to N230.6bn of the same period in the previous month. The CBN executed an aggressive strategy to mop up liquidity with the frequency of OMO auctions. However, although the frequency of OMO auctions where high, the volume was not enough to completely mop up liquidity in the market. FAAC payments disbursed in the second half of the month was N299.74bn (a 13% decline from March allocations). There were also refunds of excess position for forex as well as no cash reserve ratio (CRR) debits. Hence, liquidity in the market was sustained.

Short-term interbank rates (OBB, O/N AND 30-DAY rates) averaged 4.93% p.a. in the second half of April. This is 380bps lower than that of the corresponding period in March with an average of 8.73%. This is as a result of interest rates moving in tandem with the liquidity in the system. As at April 29th, the OBB and O/N rates were at 3.08% p.a. and 3.67% p.a. respectively. These rates are up 250bps and 275bps from their respective figures in the end of March.

Chart 1: NIBOR % p.a.



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Outlook

Following the expected approval of the 2016 budget in May, there would be increased liquidity into the economy. In addition, the monthly statutory allocation to be shared in May would be higher due to the uptick in oil prices recorded in March/April. The CBN is expected to continue with its interventions to manage market liquidity. The MPC is meeting on May 23/24. If April inflation numbers increase further, there is a possibility of a further monetary policy tightening. If this happens, other interest rates would move in tandem.

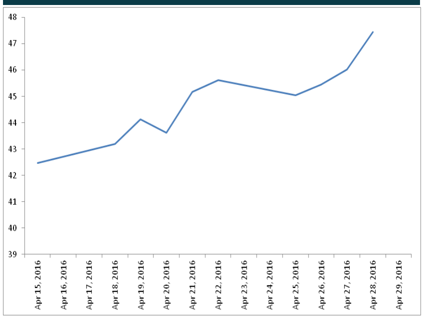
15 Source: FDC Think Tank, CBN database

Oil Market

Oil Prices

Global oil prices (Brent crude) averaged $45.09pb between April 15th – April 29th, 2016, 11.83% higher than the average of $40.32pb in the second half of March. The April 17 meeting in Doha ended in a "no deal". However this had a marginal effect on oil prices. As at the end of April, Brent crude traded at $48pb, the highest level YTD. This can be attributed to a decline in US oil production to 8.94 million barrels a day last week, the least since October 2014 according to Energy Information Administration data. The World Bank has revised upwards its 2016 global forecast for oil prices to an average of $41pb from $37pb earlier projected.

Chart 2: Brent Crude Oil ($/b)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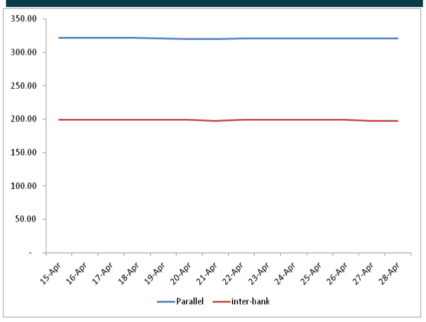
Outlook

Standard & Poor recently downgraded Exxon Mobil's AAA credit rating to AA+ due to its reservations about the company meeting expectations, given low oil prices. This signals that Exxon Mobil's borrowing costs would increase, affecting its profitability. The downgrade reflects the dire state oil companies are in due to the plunge in oil prices and may indicate a possible fold up of fringe players. Banks are likely to be more hesitant to lend to the oil and gas sector, which would affect investment prospects and profitability. OPEC would be meeting on June 2 for its bi-annual meeting. Deliberation of a possible output freeze is still on the table as Iran is projected to have reached its pre-sanction levels in June.

Chart 3: Forex (N/$)



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Forex Market

The naira was stable at both the interbank and parallel markets. As at April 29th, the naira traded at N321/$ at the parallel market, a slight 0.3% appreciation from N322/$ on April 15th. The interbank foreign exchange market (IFEM) experienced a less subtle appreciation of 0.72% to N197.43/$ on the 29th of April compared to N198.88/$ on April 15thThe IATA rate of exchange remained flat at N200/$ during the same period under review.

16 Bloomberg
17 CBN, FDC Think Tank

Outlook

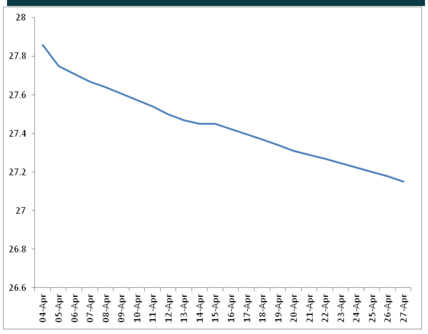
Although the volatility seen in the market earlier in the year has subsided, the fundamentals remain the same. The demand pressure on the dollar is expected to intensify once the budget has been signed by the President. With inflation estimated to increase further in April and the lingering fuel scarcity and economic deterioration, the President and the CBN are likely to lean towards a more favorable exchange rate policy. The possibility of a dual exchange rate adopted at the next MPC meeting is high.

External Reserves

External reserves are down by 1.35% to $27.09bn as at April 29th from $27.45bn as at the start of the second half of month. Year to date, the reserves level has declined by 6.52% ($1.89bn).

The external reserves level is 21.5% below 2015's peak of $34.51bn and 12.3% lower than 2015's average of $30.89bn. The level of import and payments cover is down to 4.38 months from 4.44months on April 15th.

Chart 4: External Reserves($ 'bn)



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Outlook

There is a time lag between when movements in oil prices feed into the level of external reserves. The sustained increase in oil prices is expected to slow the depletion rate of the reserves level. However, the backlog of unpaid remittances is in excess of $500m. if a currency adjustment or flexible exchange rate policy is adopted this may halt the decline in external reserves

18 FDC Think Tank and CBN database

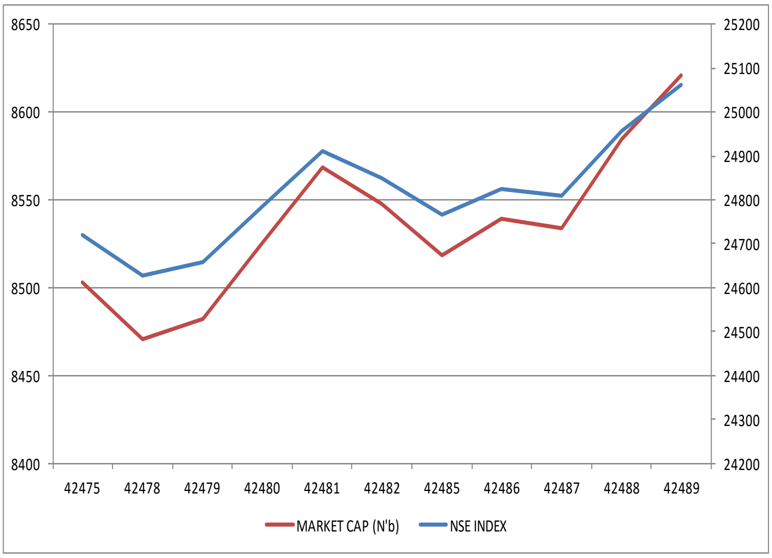
Stock Market Update

First Quarter 2016 results and full year 2015 results released in the last two weeks of April had a marginal effect on the activities in the Nigerian Stock Exchange (NSE). The market remained indifferent to the rally in crude prices as investors remained wary of a worsening risk environment.

Although only 15 stocks are exposed to the MSCI EM Index, investors have remained apprehensive since Morgan Stanley threatened to remove Nigeria from the Frontiers index. The anxiety was palpable as the share prices of the affected stocks declined in the review period despite reassurances from the NSE that the MSCI would not take any surprise actions.

The Nigerian Stock Exchange (NSE) All Share Index ASI closed at 25,062.41 up 1.39% from 24,719.27 in the first half of the month. Market capitalization also increased by 1.39% in the last two weeks of April from N8.50 trillion to N8.62 trillion. Year-to-date (YTD) return on the market however remained in negative territory of (12.50%).

Chart 5 : NSE Performance



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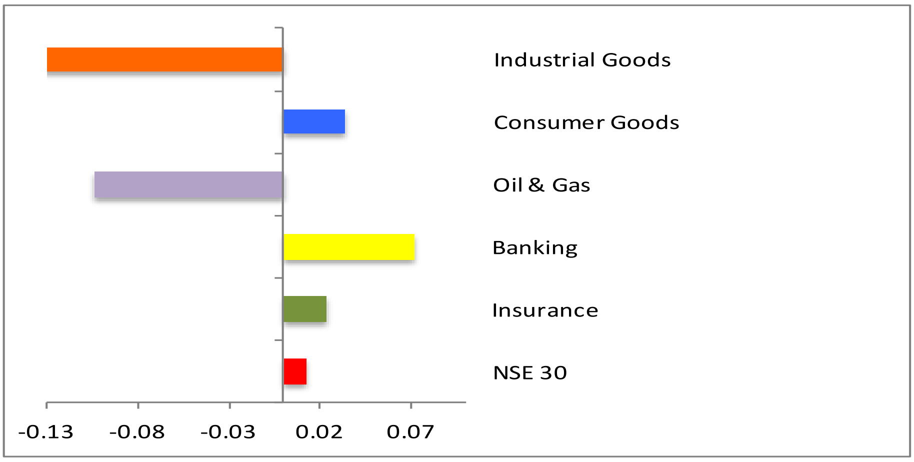
19 Source: NSE, FDC Think Tank

Gains in the share prices of Zenith Bank Plc 10.92%, Access Bank Plc 9.76% and Wema Bank 14.29% nudged the financial services sector up by 7.21% making it the best performing sector during the period under review.

The Consumer Goods sector also appreciated by 3.23% on the back of the positive performance of Tiger Branded Consumer Goods and A. G. Leventis Plc.

A 23.05% drop in the share price of Forte Oil saw the Oil and Gas sector shed 10.35% recording the worst sectoral performance in the last two weeks of April. Industrial goods also shed 2.00% as Portland Paints and Larfarge Africa shed (16.67%) and (8.12%) respectively.

Chart 6 : Bi-Monthly Sectoral Performance



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Sectoral Analysis

The financial services sector dominated activities on the exchange during the period under review accounting for 63.86% of the total value traded. The consumer goods sector accounted for 20.23% whilst industrial goods, oil & gas and conglomerates sector accounted for 9.95%, 3.75% and 1.07% respectively. Total value of goods traded within the period was N6.35bn while market breadth

20 Source: NSE, FDC Think Tank

increased to 1.11x as 41 stocks advanced against 37 stocks that declined. 112 stocks remained unchanged during the period under review.

The best performing stocks include Eterna Plc 41.98%, Tiger Branded Consumer Goods 31.74%, A.G Leventis 23.68%, Learn Africa 18.06% and National Salt Company of Nigeria 17.57%.

TOP GAINERS			
COMPANY	14-Apr	28-Apr	% CHANGE
ETERNA PLC	1.62	2.3	41.98%
TIGER BRANDED CONSUMER GOODS PLC	2.3	3.03	31.74%
A.G LEVENTIS NIGERIA PLC	0.76	0.94	23.68%
LEARN AFRICA PLC	0.72	0.85	18.06%
NATIONAL SALT. NIG. PLC	7.4	8.7	17.57%

Top losers during the period were; Airline Services and Logistics -26.50%, Forte Oil -23.05%, Law Union and Rock Insurance -18.03%, Portland Paints and Products -16.67%, Fidelity Bank Plc -16.43%.

TOP LOSERS			
COMPANY	14-Apr	28-Apr	% CHANGE
ETERNA PLC	1.62	2.3	41.98%
TIGER BRANDED CONSUMER GOODS PLC	2.3	3.03	31.74%
A.G LEVENTIS NIGERIA PLC	0.76	0.94	23.68%
LEARN AFRICA PLC	0.72	0.85	18.06%
NATIONAL SALT. NIG. PLC	7.4	8.7	17.57%

Corporate Disclosures

Asides Union Bank and Access Bank Plc, Profit Before Tax (PBT) and Profit after Tax (PAT) for all other banks who have released results dropped. PBT has dropped by an average of (8.70%) whilst average drop in PAT came to (6.50%)

	% Change In Gross Earnings	% Change Net Interest Income	% Change Net Impairment Charge	% Change Net Fees & Commissions	% Change PBT	% Change PAT
ACCESS	4.53%	46.75%	-37.99%	86.72%	36.72%	42.08%
UBA	-10.79%	11.82%	-57.17%	11.17%	-1.66%	0.18%
ZENITH	-12.25%	36.42%	23.30%	-9.01%	-3.04%	-4.00%
FIDELITY	-5.52%	30.00%	-27.55%	-0.18%	-14.54%	-10.49%
STERLING	-6.32%	24.75%	54.25%	-26.60%	-30.56%	-35.00%
FCMB	-12.19%	-4.98%	67.78%	11.34%	-61.74%	-68.82%[21]

COMPANY	REVENUE (N'bn)	% CHANGE	PAT (N'bn)	% CHANGE
MRS OIL	N25.07	17.50%	N0.626	185.30%
SEPLAT	N16.58	-35.12%	(N2.97)	-161.70%
CCNN	N3.57	-19.50%	N0.243	-61.60%
CAP PLC	N1.84	2..2%	N0.422	-13.21%
JULIUS BERGER	N28.7	-34%	N0.251	-75.60%
TRANSCORP PLC	N13.19	32.03%	N1.206	-45.03%
eTRANZACT	N2.26bn	9.06%	N0.153	-4.99%
TOTAL NIGERIA PLC	N59.7	-0.56%	N2.82	529.80%
LIVESTOCK PLC	N2.09	11.75%	N0.002	-83.17%
UACN PLC	N17.5bn	-1.19%	N1.31	-23.06%
FIDSON PLC	N1.21	-0.94%	N0.028	-31.63%
BERGER PAINT PLC	N0.76	7.67%	N0.024	-66%[22]

Profit after tax also dropped across sectors reflecting a worsening macro economic environment. Consumer goods sector was weighed down by challenges in sourcing foreign exchange for importation of raw materials and reduced disposable income just as the lull in construction activities affected companies in the manufacturing sector.

Outlook

We expect the Nigerian stock market to record marginal gains in the first half of May. Hopes on passage of the budget, and the non-removal of Nigeria from the MSCI emerging markets index is expected to bolster market confidence.

[21] Source : NSE

[22] Source : NSE

Increased speculation may increase activities on the bourse as bargain hunters take advantage of stocks that were oversold before the release Q1 results.

Corporate Focus—United Bank for Africa Plc (UBA)

Analysts Recommendation: BUY

Recommendation Period: 365 days

Target Price: N5.31

Analyst's Note

With oil prices still low despite slight recoveries in recent weeks, Nigeria's economy continues to go through turbulent times as creeping inflation, forex uncertainty, rising unemployment and bleak economic prospects persist. The banking industry is one sector that has fallen victim to the persistent macroeconomic headwinds that have weakened consumer purchasing powers and eroded earnings of companies including banks. Nigerian banks are grappling with reduced credit growth due to lower loan demand, higher impairments from oil & gas exposures, and increasing regulatory capital requirements. The Nigerian bourse All Share Index has lost over 12% YTD; just the banking sector index has declined 7.7% YTD. Various banks issued profit warnings prior to the release of their FY 2015 results.

In spite of all these adverse conditions, UBA has shown its resilience as reflected in ability to maintain profitability and ensure a high asset quality. Its PAT increased by 24.5% in FY 2015 and remained flat in Q1'16. The bank also maintained its non-performing loan ratio (NPL) at 1.7%, an industry benchmark. UBA's superior risk management framework helped ensure subdued impairment effects from oil & gas exposures. Its share price has declined by about 20% due to investor concern and pervading economic uncertainty. Given UBA's revenue potential, recent performance, extensive network and branch system, large customer base, robust risk management framework and exceptional management, it is a company with an immense upside. Accordingly, we place a BUY rating on the stock.

Profile

UBA Plc is a leading African bank headquartered in Lagos, Nigeria with branches across Africa, Europe and America. UBA commenced operations as the British and French Bank Limited (BFB) in 1949 before it was incorporated as a limited liability company on 23 February 1961. Listed on the Nigerian Stock Exchange in 1970, it is the first Nigerian bank to make an Initial Public Offer and issue Global Depositary Receipts (GDRs).

Following its merger with Standard Trust Bank in 2005, UBA has pursued a pan-African expansion mission, which has seen it have branches in 19 African countries including Ghana, Kenya and Tanzania. The banking group provides corporate, commercial, SME, consumer finance and personal (retail) banking services to over 8 million customers through diverse channels including online banking, mobile banking, ATMs and social media.

UBA's growth through the years can be seen in key financial metrics between 2011 and 2015. During that period, total assets and shareholders (attributable to owners) have grown by a CAGR of 9.4% and 21.9%, respectively. Net interest income has also grown by a CAGR of 19.3% while net income grew by a CAGR of 5% between 2012 and 2015, after recording a loss in 2011.

United Bank for Africa (NGN'mn)	2011	2012	2013	2014	2015	CAGR
Gross loans to customers	605,627	658,922	937,620	1,071,859	1,036,637	14.4%
Net loans to customers	581,174	643,117	918,293	1,048,348	1,010,855	14.8%
Interest earning assets	1,670,982	1,880,732	2,169,212	2,155,756	2,237,635	7.6%
Total assets	**1,920,435**	**2,272,923**	**2,642,296**	**2,762,573**	**2,752,622**	9.4%
Deposit from customers	1,445,822	1,720,008	2,161,182	2,169,663	2,081,704	9.5%
Deposit from banks	19,510	57,780	60,582	59,228	61,066	33.0%
Interest bearing liabilities	1,602,372	1,892,308	2,270,630	2,342,688	2,272,666	9.1%
Total liabilities	**1,769,495**	**2,080,456**	**2,407,260**	**2,497,167**	**2,420,001**	8.1%
Shareholders equity (attributable to owners	**147,345**	**189,106**	**227,647**	**259,930**	**325,827**	21.9%
Interest Income	113,590	150,003	185,700	196,680	233,969	19.8%
Interest expense	45,423	58,386	82,469	90,547	96,030	20.6%
Net interest income	68,167	91,617	103,231	106,133	137,939	19.3%
Net fee and commission income	38,660	45,108	44,874	47,966	53,335	8.4%
Profit before tax	(26,600)	52,010	56,058	56,200	68,454	NA
Taxation	(17,935)	533	9,457	8,293	8,800	NA
Net profit	**(8,665)**	**51,477**	**46,601**	**47,907**	**59,654**	5.0%

Source: UBA Plc Annual Reports

UBA's tremendous growth into becoming one of the dominant financial services institutions in Africa has been propelled by its driven and talented management team. Chaired by the visionary Mr. Tony Elumelu, the board of directors comprises accomplished professionals from varied sectors of the economy.

Mr. Elumelu is a renowned economist, investment guru, entrepreneur and philanthropist. He has been instrumental in turning UBA into one of the most successful pan-African banking hubs in Africa. In 2011, via his private holding company, Heirs Holdings, Mr. Elumelu was able to acquire conglomerate giant Transcorp. Beyond his business interests, Mr. Elumelu advises and holds seats in public and social sector boards such as the United Nations Sustainable Energy for All Initiative, Private Capital Group for Africa (PCGA) Partners Forum, and the Agricultural Transformation Implementation Council (ATIC). He serves as vice-chairman on the National Competitive Council of Nigeria (NCCN), is chairman at Transcorp, and co-chair at the Aspen Institute Dialogue Series on Global Food Security. Mr. Elumelu has two degrees in economics with a BA from the Ambrose Alli University and a Masters degree from the University of Lagos.

Phillips Oduoza currently serves as the Group Managing Director of UBA. Prior to this appointment, he was the Deputy Managing Director of UBA Plc responsible for banking business in the south of Nigeria. He is a banking veteran with a twenty-year banking career. He holds a first class degree in civil engineering and an MBA (finance), both from the University of Lagos. The renowned banker is an honorary fellow of the Chartered Institutes of Bankers.

Kennedy Uzoka is the Deputy Managing Director/ CEO of UBA Africa. He will take over from Phillip Oduoza as UBA's Group Managing Director in August 2016. His experience in managing UBA's African business positions him towards driving the company to achieve its next growth phase: being the leading financial services franchises in Africa. Mr Uzoka's career with UBA started with his supervision of the Bank's operations in New York and London. He headed the strategy and business transformation of UBA group before going on as regional bank head of the south bank of Nigeria covering over 17 states. With UBA he was also Regional Director, South East, Vice President, Northern Nigeria, Chief Marketing Officer, Federal Capital Territory (FCT), Chief Marketing Officer, Lagos, and later he served as Managing Executive Officer at STB (before merger with UBA). He holds a BSc in mechanical engineering from the University of Benin as well as an MBA from the University of Lagos.

With the abundance of high-performing professionals leading its evolution into becoming an African banking behemoth, UBA is positioned towards actualizing its immense potential even beyond Africa. The ability of UBA's management team to steer the bank towards profitability in both FY 2015 and Q1'2016 while managing its loan book risks, underscores the depth of its skilled management team

The Bulls Say and the Bears Say

Bulls Say:

- Varied product range tailored to a diversified customer base
- Diversification of the Nigerian economy beyond the oil & gas sector provides banks with an opportunity to benefit from potential high-growth sectors
- Experienced and talented workforce
- Reduced risk of asset impairment as the bank's exposure to the oil & gas sector is below industry average
- Enhanced risk management framework
- Superior brand value

Bears Say:

- Higher impairment risk due to exposures to the oil & gas and power sectors
    - Persistent macroeconomic headwinds have reduced the bank's ability to grow its loan books and asset base
- Increasing regulatory requirements, which could negatively impact interest income and earnings

- Intense competition for customers and talent in the banking industry
- Customers are increasingly demanding for excellent service at lower cost

Investment Thesis

FDC places a BUY recommendation on UBA Plc based on an analysis of the bank's interest earning potential, asset quality, rising interest rate environment, expansion strategy and favorable regulatory policies aimed at ensuring stability in the financial system. Though the downturn in the oil & gas sector has led many banks to impair loan assets belonging to oil & gas firms that have issued servicing their obligations, UBA's total oil & gas exposure of 19.2% has limited its asset write-offs on its loan books. Its non-performing loan (NPL) ratio of 1.7% is one of the lowest in the banking industry, and it underscores the bank's commitment to a sophisticated and enhanced risk management structure. Though more than half of UBA's oil & gas exposures are to the troubled upstream sector, they are to large international oil firms and a good number of the loans have been restructured.

Furthermore, with yields on government securities increasing due to the adoption of a tighter monetary policy, UBA stands to gain from its investment securities. Additionally, a possible hike of the MPR due to inflationary pressures would lead to a high interest rate environment, thereby positioning the bank to benefit though increased interest income. As the regulatory bodies become concerned about financial system stability, we expect less stringent regulations that could affect banking profitability. The introduction of the negotiable current account maintenance fee reflects the CBN's desire to maintain a stable financial system. This fee mitigates the loss of fee and commission income due to the implementation of zero commission on turnover (COT) fees. UBA's Q1'16 result shows an 11.2% increase in net fee and commission income. The combination of the economic and banking system factor, alongside the UBA's strategic expansion drive, shows that UBA is a company with a significant upside.

%	2016E	2017E	2018E	2019E	2020E
Net Interest Margin	6.1%	5.7%	5.9%	6.0%	5.6%
Gross Yield	10.3%	10.2%	10.2%	10.2%	9.8%
Cost of Funding	4.0%	4.3%	4.2%	4.2%	4.1%
RoAA	1.8%	1.8%	2.0%	2.2%	2.1%
RoAE	14.3%	14.3%	14.8%	15.8%	14.7%
Dividend Payout Ratio	27.3%	27.3%	27.3%	27.3%	27.3%
NPL Ratio	1.8%	1.7%	1.7%	1.7%	1.7%

Valuation

We derived our valuation for United Bank for Africa Plc using the dividend discount model (DDM) method. Our fair value estimate for UBA Plc is **N5.31**, which is a 56.2% upside on its current share price of N3.40 as at 09 May, 2016. The discount rate used in the DDM is the cost of equity (20.7%), which is computed via the capital asset pricing model (CAPM). The terminal P/BV, which is factored into calculating for exit multiple, was derived using the formula (Return on Equity (ROE) – Net Income Growth)/ (Cost of Equity – Net Income Growth). The intuition behind using this formula is considering how much of UBA's ROE is being allocated to grow dividends and how much does it cost. Based on this intrinsic valuation, UBA is an undervalued stock with a potential for significant appreciation.

In forecasting UBA's assets and earnings, we took into account the low oil price environment, possible devaluation and the overall macroeconomic condition. These issues, alongside Nigeria's monetary policy uncertainty, are major investor concerns.

United Bank for Africa Plc NGNmn	2016E	2017E	2018E	2019E	2020E
Dividends	13,658	15,240	17,629	21,088	21,952
Discount period	1	2	3	4	5
PV of Dividends	11,320	10,470	10,038	9,952	8,587
Equity	369,785	411,255	459,224	516,604	576,336
Terminal Value:					
Terminal P/BV	0.64				
Terminal Value (Exit Multiple	369,993				
PV of Terminal Value	144,730				
PV of Dividends	50,367				
Present Value (NGNmn)	195,097				
Shares outstanding (mn)	36,729				
Share price (NGN)	**5.31**				

Risk

The major risks facing UBA include higher impairments due to weaker economic prospects, reduction in interest and non-interest revenues, possible devaluation and forex uncertainty, adverse regulatory requirements and increased investor concern. These risk factors could potentially reduce UBA's earnings, deteriorate its asset quality and lead to a plunge in share prices.

Persistently low oil prices could lead to a further impairment of UBA's oil & gas loans. Besides its impact on oil & gas companies, the low oil price regime has impeded economic growth, thereby hampering banks' ability to grow loans. UBA also has one of the highest exposures to the power sector (9.8%). The power sector is having issues due the use of foreign exchange in acquiring the power companies and assets. These transactions were funded mainly by banks, and the loans to these power firms may have to be impaired, especially with a currency adjustment looming. Furthermore, some stifling regulations such as the revision of Basel 2 guidelines and a possible review of certain fees, could strain the bank's capital structure and its revenue base.

While these risks pose a challenge to the bank's revenue and profitability, the bank's management team has shown that it has the appropriate risk management structure to handle adverse economic conditions. The quality of UBA's loan asset and its solid NPL ratio are impressive. The bank's capital adequacy ratio (CAR) of 20% and its Tier 1 ratio of 16% indicate adequate capital buffer. Furthermore, with oil prices recovering and projected to average at over $50 by year end, there is a possibility of reduced impairment of oil & gas loan assets. A recovery in economic growth would also boost investor confidence. In sum, UBA is well-placed to withstand shocks arising from the overall economy or banking industry.