Global Asset Allocation Report: Nigeria

First Half 2005

ARM Investment Managers

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Review of 2004 & Outlook for 2005

ECONOMIC GROWTH

Ever rising non-oil imports, coupled with our expectation for slower growth in oil exports, suggests that net exports will prove less of a growth driver in 2005 than 2004. Record high oil prices and production in 2004 have significantly increased Nigeria's GDP base - thus creating a high hurdle rate for growth over coming years. From the foregoing, we are somewhat skeptical of the government's ability to achieve the 6 - 7% target set in the proposed 2005 budget, believing that growth is likely to be slightly muted. **Thus we see 2005 GDP growth in the region of 4 - 5.5%.**

INFLATION & INTEREST RATES

The recent fuel price hike, and uncertainty regarding the future direction of crude prices (both global and domestic), coupled with the increased government spending over the coming year raise concern regarding the attainment of the Federal Government's target inflation rate of not more than 10% in 2005. **Our forecast range for consumer price inflation as measured by the 12 - month moving average is 10 - 16%.** In view of the huge funds inflow into the banking system following the CBN's reform agenda, in addition to the spending of some of the excess oil revenues over the coming year, we expect **an overall decline in interest rates.** This remains our view even in the event of limited sterilization through the CBN's resumption of the withdrawal of public sector funds from the banking system.

CURRENCY

With oil prices set to remain over US$30/barrel in 2005, the outlook for the Naira in 2005 appears positive as it gives the CBN the ability to maintain support for the currency. **We expect the Naira to hold steady against the dollar with the possibility of a slight appreciation, and forecast a support/ resistance level for ₦/USD of 136-145 in the parallel market.**

EQUITY MARKET

Whilst the macro-economic landscape appears positive for the equity market, we express concern regarding the technical factors, which traditionally, have greater impact on equity returns. Our stock picks are **Guinness, First Bank, Union Bank, Oando Plc, Ashaka, Total, UACN Nigeria, Afribank, Nestle Nigeria Plc, Zenith International Bank Plc and Guaranty Trust Bank.**

For H1 2005, our recommended asset allocation for a typical growth portfolio at **70% Equities** and **30% Fixed Income**.

ECONOMIC GROWTH - AGAIN BENEFITING FROM HIGH GLOBAL CRUDE OIL PRICES, AND TO A SMALLER EXTENT, GOVERNMENT SPENDING

With the long legacy of poor overall macroeconomic management, achieving macroeconomic stability and sustainable growth in Nigeria continues to pose a formidable challenge. Real GDP growth accelerated in 2003 due to higher oil production and rising crude oil prices as a result of the crisis in Iraq. On the flip side however, Nigeria's crude oil exploration has had severe environmental impact[1]; this has led to the emergence of various militia groups particularly within the Niger Delta Region, frequent disruptions of onshore oil production by host communities, shutting down of drilling operations in oil fields by multinational oil producing companies and attendant revenue loss to the companies and, by implication, to the Federal Government. Despite the dominant role of the petroleum sector as the major foreign exchange earner, agriculture remains the mainstay of Nigeria's economy. It is the largest non-oil export earner, the largest employer of labour, and a key contributor to wealth creation and poverty alleviation. The current administration has made some progress in the agricultural sector, which continued to exhibit strong growth[2] in 2004. Nigeria is now the world's largest producer of cassava due to new initiatives undertaken in agriculture, and also the impact of tractor, fertilizer and buyer-of-last-resort programmes that target excess produce during harvest. While the fertilizer and tractor programme transmits a 25% subsidy to farmers, the buyer-of-last-resort programme guarantees farmers a profitable floor price for their excess product.

As at September 2004, the government had released N284bln or 81% of the capital budget into the central CBN account where it is readily accessible to Implementing Agencies who have met the due process requirements. However, of the capital budget of₦350bln, only about 50% or₦175bln has been utilized or committed to date - relative to a 25% utilization rate as at mid year. Though the Federal Government estimates that in spite of the late start to the budget, the 100% target implementation rate for capital expenditures will be attained, given the bureaucracy involved, we do not think this is realizable, and consequently expect a lower contribution of government spending to economic growth than previously anticipated. As a result of the settlement of domestic public sector payment arrears as provided for in the 2004 budget (₦37bln so far this year), in addition to higher public expenditure, we are of the opinion that fiscal policy likely boosted growth in 2004, albeit to a lower extent than we had earlier expected, and as provided in the budget due to the late execution of the budget and stringent screening exercises of the due process committee.

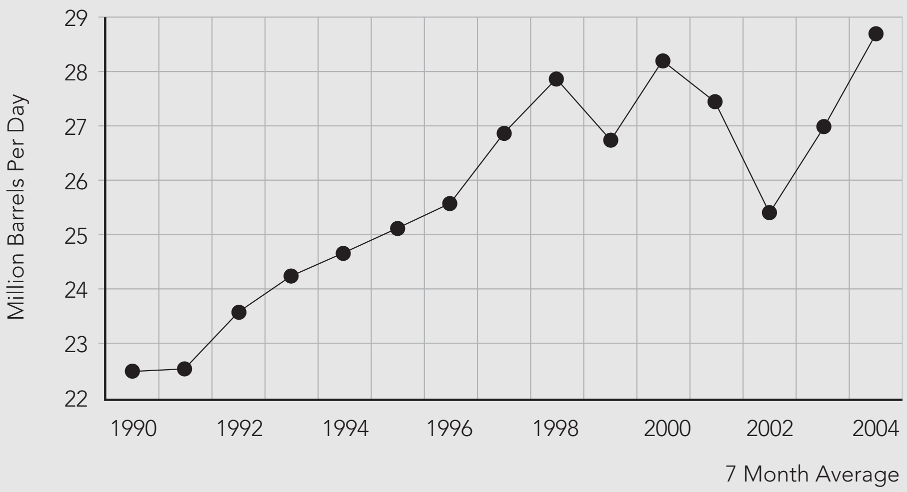
MANUFACTURING SECTOR REMAINED A LAGGARD

About 30% of the 30 manufacturing sub-sectors covered by a CBN survey operated at over 50% of their installed capacity in 2003, and these were mainly import-dependent sub-sectors. This was attributed to the poor state of infrastructure, in addition to low demand for domestic products and high demand for imports. Reflecting this, capacity utilization rose a marginal 1.9% from 44.3% in 2002 to 46.2% in 2003. Power generation, transmission and distribution initially improved to 4500MW compared to 4200MW in 2003 and 2000 MW in 1999. The government expects additional generation capacity of up to 1400 MW to come on stream by 2006 through several major investments undertaken. Following steadier power supply in many areas earlier on in the year, power generation subsequently deteriorated in the last quarter of the year, with long periods of outages becoming the norm. Overall productivity in the Nigerian industrial sector has remained low for several reasons, including:

[1] These include marine pollution, devastation of farmlands and rivers caused by acid rain due to oil exploration and gas flaring.

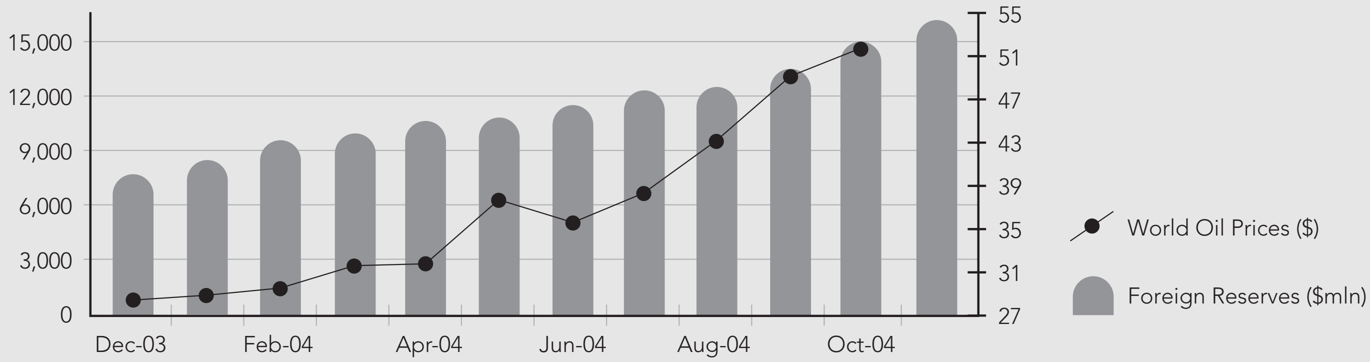
[2] The federal government estimated a 7% growth in the sector in 2004.

FIGURE 1: Total OPEC Production (1990 - 2004)



Source: www.iea.org

FIGURE 2: Rising oil prices fuelling strong growth in Foreign Reserves



Source: Central Bank of Nigeria Monthly Reports, Bloomberg

- low-technology deployment;
- low capacity utilization;
- uncertain macroeconomic and policy environment;
- inconsistent policies and frequent policy reversals;
- limited investment to modernize existing plant and machinery, and even less so in up-grading the production technology
- inadequate infrastructure, especially power and energy; and
- low skill level of workers.

Further aggravating the plight of the manufacturing sector in the third quarter of the year was the 4-day strike action by Nigerian Labour Congress in protest of the recent fuel price hike. This led to considerable losses in the sector as a result of:

- disrupted production processes
- massive manpower loss
- additional interest charges as a result of prolonged period of the transactions for investors who borrowed from the banks
- loss of perishable products imported into the country, but not yet discharged at the ports.

- breach of contractual agreements with severe penalty clauses.

A combination of the above factors kept the performance of the manufacturing sector at subpar levels over the year; further eroding the already low contribution of manufacturing to GDP growth for 2004. On balance, net exports, as a result of the dominance of oil relative to non-oil exports, in addition to record high oil prices and production, was probably the largest contributor to economic growth. Also contributing positively to economic growth over the period, albeit to a smaller extent, was government spending. On the flip side, we see consumer spending, negatively impacted by high unemployment, inflation, the subsequent erosion of purchasing power and cutback in discretionary spending, contributing minimally to overall growth in 2004. The foregoing, in addition to expectations for strong growth in the agriculture and the services sectors, including telecommunications, underscores our anticipation that growth in 2004 will, at the minimum, meet the government's 5% target.

EXTERNAL SECTOR: AS GOOD AS IT GETS?

In our July 2004 report, our expectation, predicated on the assumption that there were no disruptions to oil production in the Middle East or elsewhere, was for a modest trend toward more normal crude stock levels in the countries of the Organization for Economic Cooperation and Development (OECD), and by implication, slight moderation in oil prices. Contrary to our expectations, crude oil prices hit successive highs over the period and culminated in an all time high of $55.43 per barrel in September. Global oil prices remained high even though OPEC crude oil production reached its highest levels in September since OPEC quotas were established in 1982 largely due to increased Iraqi production (see Fig 1). Continued strong demand, especially from China, and a thin cushion of excess production and refining capacity, significantly pushed up the long-term equilibrium price of crude oil[3]. The narrow cushion of excess supply consequently produced large jumps in price in response to any reduction in supply. Hurricane-induced reductions in supply in the Gulf of Mexico (about 500,000 bpd), and threats of supply disruption in Nigeria, in addition to concerns over low winter heating fuel supplies in the US, contributed to the hike in crude oil prices. OPEC quotas, following an initial decline at the beginning of the year, have increased thrice; taking both Nigeria and total OPEC production from 2.018mln bpd and 24.5mln as at the beginning of the year to 2.224mln bpd and 27mln bpd respectively.

Due to favourable terms of trade, the external current account deficit has continued to narrow and external reserves now stand at $16.1bln; exceeding the $8.4bln target for the full year (see fig 2). The balance of trade improved substantially reflecting these developments in the oil sector, as performance of the non-oil sector showed only marginal improvement. With international oil prices remaining significantly above their historical averages, we anticipate further rise in gross international reserves during the remaining months of 2004 and see increasing likelihood of the external current account deficit moving into a small surplus.

Globally, foreign direct investment (FDI)[4] in 2003 declined 18% to $560bln from $679bln in 2002; driven by the slow and irregular pace of economic recovery in the developed world, which dominates overall FDI totals. In the developing world, though Africa and the Asia-Pacific gained, the changes were unequal even within continents; African countries rich in natural resources such as Morocco, Angola, Equatorial Guinea, Nigeria and Sudan, attracted the bulk of the increased FDI to the continent - a total of $15bln. Nigeria was the fifth African country to benefit from FDI flow, with $1.2bln in 2003 and $1.3bln

[3] Source: Energy Information Administration
[4] Source: 2004 World Investment Report

in 2002[5]. Rough estimates by the Federal Government indicate that as at September 2004, close to $1bln in new investments had come into the non-oil sectors mainly in the Foods, Beverages, Leather Goods, Power Generation, Personal Care and Pharmaceutical sectors.

THE NAIRA REMAINED STABLE

The Naira remained stable against the US$ over the second half of the year, trading within a narrow band of ₦138 and ₦142. The Naira has essentially remained indexed to the dollar as Nigeria's monetary authorities try to influence the demand/supply dynamics within the Dutch Auction System. Despite increased demand for foreign exchange as a result of the ability of independent oil marketers to import their own products, high global oil prices, strong export volumes and foreign reserves averted depreciation pressure on the currency. We see the application of substantial fiscal savings from excess crude oil proceeds continuing to provide support for the currency during the remaining months of the year and going into 2005.

PRUDENCE REMAINS THE STANDARD FOR FISCAL POLICY

The fiscal restraint that began in the last quarter of 2003 continued in 2004, with considerable oil savings signaling a reversal of the expansionary policies of the past. As at the end of November 2004, savings in the excess crude account amounted to about ₦691bln ($5.2bln); exceeding Federal Government projections of total savings of about ₦609bln by year end. Reforms to enhance oil sector efficiency, public sector transparency and accountability, fight corruption, and strengthen the financial sector have been initiated. Progress has been made in strengthening the federal budget process, reducing nonpriority outlays, and increasing investments in key priority areas in line with the National Economic Empowerment Development Strategies' (NEEDS) objectives, such as education, health, agriculture, water, and electricity. Due process and procurement reforms continued to yield dividends, thereby contributing to improving the quality of investment programs and reducing corruption in the contract system. Ministries and federal parastatals, in defence of their performance in the 2004 budget, have, however, pointed accusing fingers at the Budget Monitoring and Price Intelligence Unit (The Due Process Office); arguing that its extremely rigid conditions were frustrating the successful implementation of budgets. Given the institutionalization of corruption and rent seeking in Nigeria however, we are in agreement with the insistence from the Due Process Office that its actions were to restore discipline and order to the system of contract awards and implementation. Reflecting the prudent nature of the government's fiscal policies, the fiscal deficit as at end of September was 1.5% of GDP, well within the 2.1% target for 2004 set at an oil price of $25 per barrel.

A REVIEW OF THE 2005 BUDGET PROPOSAL

The budget, titled 'Building Physical and Human Infrastructure for Job Creation and Poverty Eradication", is the second under the National Economic Empowerment Development Strategies (NEEDS) and carries forward the work begun in budget 2004 to reform the economy and put it on the path to sustainable growth. The budget focuses on building physical and social infrastructure such as power, water, roads, education, health and security; and is based on the following assumptions:

- Crude oil production of 2.68mln bpd (including 150,000 barrels of condensate); NLNG (Nigeria Liquefied Natural Gas) and upstream gas revenues of N53bn;
- oil price of $27 per barrel;
- the continuation of a fiscal rule in which revenues above the $27 a barrel price will be saved for the rest of the year;
- joint venture cash calls of $4.23bln;
- a target inflation rate of no more than 10%;

[5] UN Conference on Trade and Development

- GDP growth rate of between 6 to 7%;
- External reserves at $15bln or 11 months of import, and
- 2004 oil income (excess crude revenues) for financing purposes of ₦158bln.

Based on these parameters, the government estimates federally collectible revenue for the year ending December 31st 2005 at ₦3.619trln of which ₦2.902trln is oil derived, ₦563bln of non-oil taxes, and ₦100bln of independent revenue. Federally retained revenue under the existing revenue sharing formula is estimated at ₦1.304trln; made up of Federal Government share of the federation account of ₦1.179trln, share of Value Added Tax of ₦25bln and independent revenue of ₦100bln. An aggregate expenditure ceiling of ₦1.618bln is being proposed. This results in a deficit of ₦314bln or 2.9% of GDP. The deficit is expected to be financed with ₦158bln of excess crude savings of 2004, privatisation proceeds of ₦4bln, sales of government property in Abuja and around the federation ₦15bln, looted fund recovery of N10bln, and access to long term funds from the capital market of ₦70bln. The total capital budget amounts to ₦531bln, a 51% increase over last year's budget of N350bln; with ₦50bln being directed at paying local contractors debts and equity of ₦10.6bln for the Nigerian Production Development Commission - one of NNPC's subsidiaries to take off. The capital budget focuses on the stated priorities of physical and human infrastructure with 33% of the budget designed for roads, water supply, power, education, health, and agriculture.

Table 1

Highlights Of The 2005 Proposed Budget			
	2005	2004	y/y % Change
Revenue (₦ trln)	1.304	1.12	16.43%
Projected Av. Oil price ($/barrel)	27	25	8.00%
Total Expenditure (₦trln)	**1.618**	**1.3**	24.46%
Projected GDP growth	6-7%	5%	higher

Source: Presidential Budget Speech

Table 2

Total Budget Allocation			
		₦ bln	% of Total
Recurrent Expenditure		651	39.31%
Capital Expenditure		531	33.62%
Foreign Debt service		170	10.51%
Domestic Debt Service		190	11.74%
Statutory Transfers			
National Judicial Council		33	2.04%
Niger Delta Development Commission	17	1.05%	
Universal Basic Education Commission	26	1.61%	
		1,618	

Source: Presidential Budget Speech

Table 3

Deficit Funding	
	₦ bln
2004 Excess Crude Oil Savings	158
Privatisation Proceeds	4
Sale of Government Property	15
Looted Fund recovery	10
Access to Long Term Funds from the Capital Market	70
Not Specified	57
Total deficit	**314**

Source: Presidential Budget Speech

On the use of the additional income from excess crude, a total of ₦609bln ($4.6bln) is projected as savings on the excess crude for the Federation Account by the end of 2004; the Federal Government's share of this savings is estimated at ₦316bln. Based on a discussion with stakeholders of the different tiers of government, it has been decided to permanently save 50% of this additional income, whilst putting 50% towards financing additional expenditures in the 2005 budget. The 50% savings is designed to cushion the volatility of revenues and expenditures based on the uncertain commodity price of oil while the 50% for additional expenditures is expected to be channelled largely towards physical and social infrastructure as follows: Agriculture (₦5bln), Power (₦18bln), Works (₦29bln), Defence (₦20bln), Police (₦7bln), Internal Affairs (₦9bln) and ₦40bln to three development banks of agriculture, industry and housing.

- Payroll and overheads amount to ₦651bln or 40% of the budget; the government has attributed the continued large size of the recurrent budget to several factors: salaries and allowances of newly recruited police, monies for capacity building of the civil service as part of the public service reforms as well as anticipated redundancy payments, and some arrears of professional allowances to teachers, doctors, researchers and others that were not paid in the past.
- Due to the weight of the new contributory pensions and mandatory life insurance, costing the Federal government a contribution of ₦44bln, pensions have increased from ₦70bln in budget 2004 to ₦119bln. Pension arrears under the Pay As You GO are large and estimated at over ₦1trln. Though implementing reforms in pensions, the public service, and the National Health Insurance Scheme have added close to ₦70bln to the 2005 budget, the medium to long-term payoffs in a functioning pension scheme and a more efficient public service justify these expenditures.
- The government proposes to continue the fiscal rule of saving all revenues above the budgeted price and deciding appropriation in a manner compatible with good economic management. This prudent budget practice will be embedded in a law increasing budget transparency, encouraging fiscal prudence, and accountability in all tiers of Government, known as **"The Fiscal Responsibility Bill"**.
- The government intends to harmonize tariffs with the ECOWAS tariff regime which consists of four tariff import bands, 0% for necessities, 5% for primary products, 15% for intermediate goods and 20% for finished products. With this policy, there will be no need for waivers and exemptions starting June 2005 and Nigeria's unweighted average tariff will adjust to 18% from a previous level of 29%.

Overall, the highly restrained fiscal stance of early 2004, which enabled the government to sterilize excess oil revenue and significantly increase international reserves, is particularly encouraging. It would appear that the government has built on the progress made on the 2004 budget process and begun the 2005 budget cycle early, strengthening the prioritization of capital projects, designing a strategy to address domestic arrears, and developing a Medium Term Economic Framework consistent with NEEDS. Given the need for prudent management of oil windfalls, which we have reiterated time and again, the adoption of the fiscal rule is a significant positive for

[1] Food and beverage sector includes 7-Up, Cadbury, Flour Mills, Nestle and Nigeria Bottling Company
[7] ARM Estimates

the economy. This will help de-couple expenditure policy from the highly volatile short-run impact of oil price movements. In addition, it provides a much-needed guidepost for sustainable public investment and consumption of oil resources, taking into account intergenerational equity concerns by committing some portions of oil revenue to future generations. In this way, expenditure is stabilised at levels consistent with long-run targets and the government can draw on the extra savings generated during boom times to sustain expenditure when oil prices are low.

Our views of the proposed budget are reflected in our outlook report for 2005.

INFLATION REMAINED HIGH OVER THE PERIOD

Achieving a single digit inflation rate, one of the economic targets of the present government, has remained elusive as inflation has been high and volatile in 2004. This was attributable to high fuel prices following the liberalization of domestic prices for petroleum products, high cost of operations, high import duty, supply bottlenecks in production activities and trade policy regime, particularly the import prohibition. Furthermore, as a result of the inability of the Federal Government to access long term funds from the bond market to finance the budget deficit, the 2004 deficit was financed through the traditional Ways and Means, which is inflationary. Overall, inflation accelerated sharply over the first half of the year, peaking at 28.99% (year-on-year) in April; subsequently, the year-on-year rate declined to 13% as at August 2004. The 12-month moving average rate however continued to rise till June, when it peaked at 19.7% before subsequently declining to 18.2% in September (see fig 3). The declines were due to favourable growth rate comparisons over the previous year and dampening effects of the harvest period on food prices, which constitute about 30% of the composite. For the rest of the year, given the September hike in prices of petroleum products on the domestic scene, we see a build up in price pressures across the economy.

TIGHTER MONETARY POLICY LED TO SLOWER GROWTH IN MONEY SUPPLY

We had earlier emphasized the need for the elimination of recourse to CBN financing of budget deficits in order to reduce the burden of monetary policy in ensuring macro-economic stability. An increasingly complex macro-economic environment has continued to create challenges for the monetary policy authority. Expansionary monetary conditions led to a

FIGURE 3: Mixed signals on the inflationary front

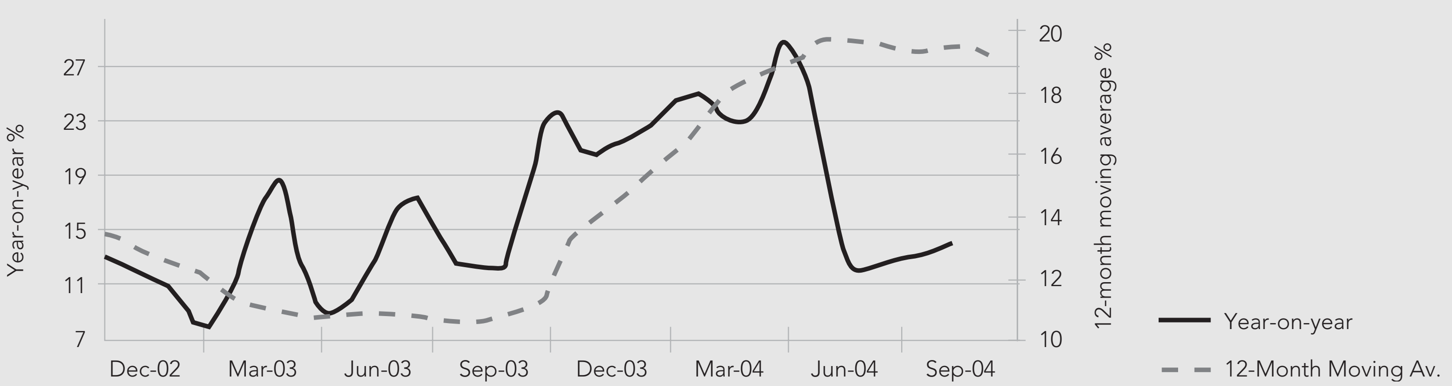


FIGURE 4: Fiscal restraint led to slower than budgeted growth in money supply

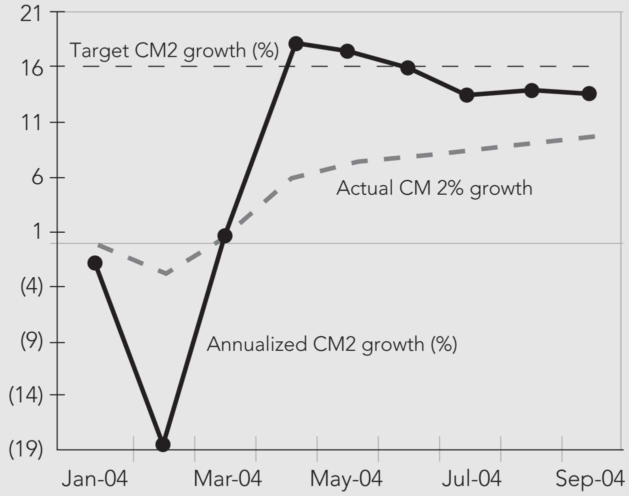
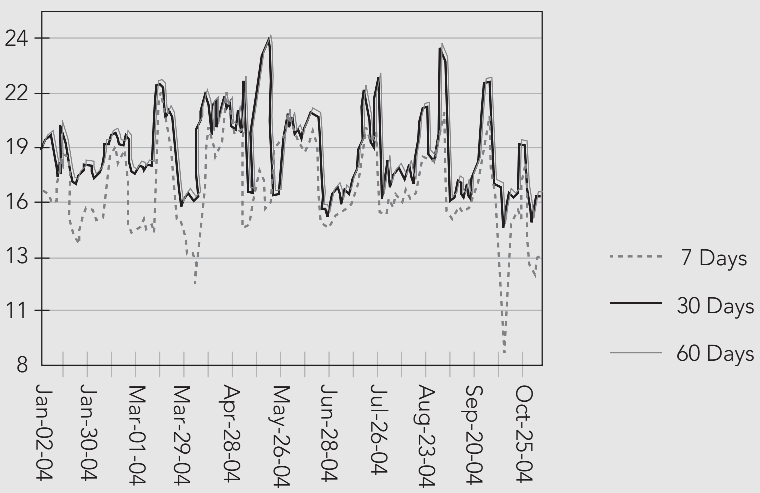


FIGURE 5: Nigerian Interbank Offer Rates traded quite volatile over the period (%)



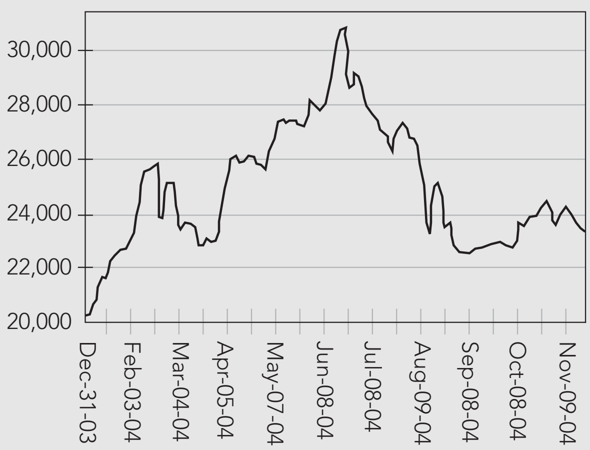
monetary overhang and negative real short-term interest rates by end-2003 and early 2004. Just as we had anticipated in our 2004 half year report, as a result of the pressure on domestic prices, and expanding bank credit to the public sector, the CBN acted proactively by tightening monetary policy in H2-04. What we had not anticipated however, was the extent of measures that would be implemented. On the 6th of July 2004, the CBN governor announced a set of reforms aimed at strengthening the banking sector through consolidation; chief amongst which was the requirement for banks to recapitalize to the tune of N25bln, up from N2bln by December 2005.

Following this, the CBN, in August, directed parastatals to withdraw their funds from banks with a view to controlling inflation, ensuring stability of the Naira through mopping excess money in the system and weaning Nigerian banks from over reliance on public sector funds. Not suprisingly, this led to scarcity of funds and near crisis in the banking system following increased difficulty in meeting depositors' demands. In addition, the CBN's shift to daily open market operations - introduced in November 2003 - helped lower excess liquidity in the banking system. As net credit to government contracted, real rates became marginally positive. The CBN subsequently suspended the withdrawal in order to enhance the stability of the financial system. As a result of the following measures, money supply growth slowed considerably over the period; broad money stock (M2) rose 9.9% in the first nine months of 2004, representing an annualized growth rate of 13.2%, compared with the permissible expansion rate of 16.0% for fiscal 2004 and significantly lower than the 23.6% rate in August 2003 (see fig 4). In line with the traditional trend, the money market traded volatile over the period (see fig 5), reflecting developments with respect to JV cash call payments as well as statutory allocations.

EQUITY MARKET: FINALLY SUCCUMBING TO THE FORCE OF GRAVITY

In our July 2004 report, we had expressed our concern regarding the sharp run up in equity prices coupled with high level of speculative activity within the equity market; arguing that in the absence of supportive fundamentals, there was a strong basis for a near-term pause in the market. Our fear then was that unless the pace of growth in earnings and economic conditions improve, the equity market would remain richly valued and susceptible to sharp declines. Following its peak in June 2004, the Nigerian All Share Index declined substantially over the second half of the year. Initially, the declines were as a result of profit taking in the wake of the market's strong performance and fund raising efforts ahead of the Guaranty Trust Bank and Zenith Bank offers. The pull back was subsequently aggravated by the afore mentioned CBN bank recapitalization directive. The immediate reaction was substantial losses within the banking sector as investors reallocated assets to highly capitalized banks given the uncertainty facing the industry and apprehension on survival prospects of smaller banks. Subsequently, the CBN directed federal parastatals to withdraw their funds from commercial banks. The resultant withdrawal of funds from the equity market by banks, both via margin accounts (largely applied to speculative activity), and direct liquidation of equity holdings, in a bid to meet the new capitalization requirement and cushion the liquidity pressure in the system, exerted downward pressure on equity prices. A combination of these measures led to a very tense atmosphere within the equity market which subsequently filtered into the money market as large banks restricted inter-bank lending to avoid the risk of getting their funds locked in smaller banks. Consequently, interbank rates trended higher, leading to even more reallocation of assets from the equity to money markets. A sharp rise in primary market activity across broad sub-sectors of the market, with particular emphasis on the banking sector, coupled with heightened interest in these primary market issues, led to investors raising liquidity from the secondary market. Other issues in addition to the Guaranty Trust Bank and Zenith

FIGURE 6: NSE All Share Index Performance



offers were Access Bank, Oceanic Bank, Oando public & rights offers, UACN Plc Rights offer, as well as various private placements. Record subscription for some of these offers (Zenith Bank - 500%), Oando Nigeria Plc (459%), and (Guaranty Trust Bank - 250%) was attributable to aggressive marketing, heightened awareness, and the performance profile of the companies. In addition, as a result of the uncertainty arising from implementation parameters of the pension reform bill, there was an upsurge in fund liquidations by many fund managers over the period which further depressed market performance.

Again, in our earlier report, our view was that given the marked rise in operational costs, healthy growth in profits might be a tall order. Over the first half of 2004, average earnings[6] across Nigerian companies have recorded a 3.77% growth rate relative to the 19.55% pace recorded over the same period last year. This mirrored, to a large extent, companies' struggle with rising operational costs induced by the high inflation environment, coupled with reduced product demand in the wake of lower consumer real incomes. Reflecting these developments, valuation levels deteriorated substantially, particularly earlier in the year as the rate of price appreciation outstripped the pace of earnings growth by a wide margin. The absence of attractive dividend and bonus announcements also provided little in form of technical support for the market. A combination of all the above factors led investors to seek safe haven investments such as fixed income and money market instruments. Following the much awaited listing of Zenith bank shares, by the beginning of the fourth quarter, there was a pick up in activity in the equity market, and sentiments improved slightly. Overall, the equity market lost 18% over the second half of the year, bringing year to date performance to 17.93[7]% (see fig 6).

Table 4: ARM H2 2005 Model Portfolio Performance

	H2 '04 Return	2004 Full Year Return
ARM Model Portfolio Return	-11.17%	30.43%
NSE-All Share Index	-19.44%	15.61%
ARM 40 Index[8]	-20.68%	22.57%
Shares	**H2-04 Returns**	
Guaranty Trust Bank	0.00%	
First Bank of Nigeria Plc	0.93%	
Union Bank of Nigeria Plc	-11.34%	
Nigerian Bottling Company	-19.43%	
UAC Nigeria Plc	0.00%	
Nestle Foods Plc	-4.50%	
Guinness Nig Plc	-32.58%	
Unilever Nigeria Plc	-12.37%	
WAPCO	-32.35%	
Oando Plc	0.00%	

[6] ARM Estimates based on half year reported earnings stripped of sharp aberrations in growth rates recorded over the first six months of the year. These were a 59% decline in after tax profits for Nigerian Breweries, which remains the most capitalized stock on the NSE All Share Index, and a 262% and 138% growth in earnings for Mobil and Oando Plc respectively.
[7] As at 30 November 2004
[8] A market value weighted Index comprising the 40 most-capitalized stocks on the NSE

Table 5: ARM H2-2004 Model Portfolio Performance Attribution Analysis

Security	Index Weight	H2 Return	Weighted Index Perf.	Portfolio Weight	Weighted Portfolio Perf.	Variance
Guaranty Trust Bank	4%	0.00%	0.00%	10%	0.00%	0.0000
First Bank of Nig	5%	0.93%	0.05%	10%	0.09%	0.0005
Union Bank Nigeria Plc	6%	-11.34%	-0.68%	10%	-1.13%	(0.0045)
Nigerian Bottling Co.	4%	-19.43%	-0.78%	10%	-1.94%	(0.0117)
UACN Nigeria Plc	1%	0.00%	0.00%	10%	0.00%	0.0000
Nestle Foods Plc	5%	-4.50%	-0.23%	10%	-0.45%	(0.0023)
Guinness Nigeria Plc	7%	-32.58%	-2.28%	10%	-3.26%	(0.0098)
Unilever Nigeria Plc	2%	-12.37%	-0.25%	10%	-1.24%	(0.0099)
WAPCO	1%	-32.35%	-0.32%	10%	-3.24%	(0.0291)
Oando Plc	3%	0.00%	0.00%	10%	0.00%	0.0000

THE BOND MARKET

The Federal Government delayed its intention to approach the capital market with another ₦40bln bond owing to the heavy traffic of activities at the capital market instigated by banks' quest to recapitalize[9]. The objectives of the bond issuance program are:

- in the short term, primarily to raise money from the capital market to finance part of the 2005 budget deficit in a more efficient and less inflationary way than the traditional practice of reliance on Ways and Means advances, which are subsequently converted to treasury bills;
- in the medium term, to provide a vehicle for restructuring the current stock of domestic debt, thus ensuring better asset-liability match; and
- to promote the development of a vibrant and efficient capital market

Over the period, the NSE listed the ₦4.6bln First Cross River State Floating Rate Redeemable Ranch Development Bond 2004/2007. With the listing, the number of state government bonds listed increased to six. Our view remains that a critical component, if not a pre-condition, to developing a bond market, is the need for macroeconomic stability and prudent fiscal and monetary framework. Another key requirement for the development of the bond market is active participation by the Federal Government in the secondary market in order to provide much needed liquidity. In addition, the duration the statutory Treasury bond holdings of commercial banks can be systematically extended. We note, however, that extending the yield curve for fixed rate instruments continues to pose a major challenge for countries with a history of weak macroeconomic policies; suggesting the need for gradual development of the yield curve, starting with the short end. We are of the opinion that a combination of these factors will encourage a more active bond market.

SMALL AND MEDIUM ENTERPRISES (SMES)

The key role that small businesses and entrepreneurs have to play in a knowledge economy has been well

[9] Banks across the country invested a total of N40.93bln representing 56.41% of total subscription of the First Federal Government 2003 N150bln bond issue

proven in other countries. In just over 20 years, India has grown from an underdeveloped socialist state into the world's second largest exporter of software. In South Korea, the new wave of small high-tech businesses have overtaken the old large firms like LG, Hyundai and Samsung to become the bedrock of the country's recovery from the Asian economic crisis. With its Vision 2020 agenda, Malaysia has transformed itself into one of the world's fastest growing economies; largely due to its focus on small businesses and their powerful contribution to economic growth.

In any country seeking to modernise, entrepreneurial activity needs well functioning capital markets able to channel finance to the most promising projects. Recent government activities in Nigeria have demonstrated that the small business sector is now seen as an integral part of Nigeria's renewal and regeneration process. We view the increasing shift of emphasis to the small business sector as a crucial step in the right direction; with globalisation and the emergence of the digital economy, small firms play a crucial role in experimentation and innovation that lead to technological change and employment growth. For Nigeria to be able to make such a successful transition, it must put in place the right conditions and encourage the right culture that stimulates a knowledge driven economy. Thus, the government needs to intensify its efforts towards fostering a strong entrepreneurial culture in which more and more innovative people can set up their own businesses thereby creating more jobs and wealth.

Among the new approaches to SME financing in the country are venture capital, the Small and Medium Equity Investment Scheme[10] (SMIEIS), and the National Credit Guarantee Fund. Although venture capital is very active in a number of developing countries, it is only beginning to emerge as a viable financing option for SMEs in Nigeria. The success of venture capital[11] in Nigeria will depend on the emergence of a new breed of knowledgeable entrepreneurs. The benefits of venture capital go beyond the provision of long-term finance; one of the numerous problems confronting SMEs was the perennial problems of inadequate managerial capacity and poor quality services and products, which compromise SMEs' success. Since they have a vested interest in the success of a business, venture capitalists, unlike banks, actively work with the company's management by contributing their experience and business knowledge gained from helping other companies with similar growth challenges. For a country like Nigeria looking to achieve real economic growth, alleviate poverty and create jobs, the potential for venture capital in helping to develop a culture of investment is phenomenal. The time is therefore ripe for Nigeria to take action by putting in place the conditions necessary for the take off of an efficient venture capital industry. These include financial infrastructure and encouraging institutional investors like pension and insurance funds to take more interest in venture capital investment, via the provision of incentives like tax benefits.

OUTLOOK

ECONOMIC GROWTH LIKELY TO MODERATE IN 2005

A central theme of Nigeria's economic reform programme is diversification of the economy to reduce dependence on the oil and gas sector, and also to stimulate a broader economic base that creates a high number and variety of employment opportunities. We view the diversification of the economy from its mono-product nature, and focus on small and medium enterprises, as the panacea for sustain-

[10] The policy objective of SMIEIS was to stimulate increased availability of capital to SMEs while reducing their debt-service burden, and also to help in the restructuring of the capital of SMEs to stimulate their revitalization and growth.
[11] Venture capital is a form of long term investment for start-up companies and growing businesses that have the potential to develop into significant economic contributors

able economic growth. The Federal Government has done a lot as far as developing a clear investment policy with respect to five priority sectors in addition to the oil and gas sector. They include agriculture, solid minerals, manufacturing, information communication technology and tourism.

The recent hike in energy costs is a key macro-economic negative from two perspectives; on one hand, companies, if unable to pass on higher input prices, would squeeze profit margins to keep volumes steady and, being less profitable, will reduce investment plans. On the other hand, we see consumers' purchasing power being eroded, either through drawing on their savings to maintain their living standards or spending less. However, since a large part of consumers' energy bills is inelastic, we expect that discretionary spending cuts will affect both imported and domestically produced goods and services. In the same vein, the continuation of the import ban, albeit somewhat ineffective with regards to protecting local industries, will keep prices of affected goods high, thereby weighing on consumer demand. This, in our view, would lead to a vicious circle where weaker demand leads companies to cut inventories and investment plans further, contributing to depress aggregate demand even more and, ultimately, economic growth.

Continued industrial action by labour, and the crisis in the Niger Delta are other factors that cast gloom on the economic outlook given the expected loss in man-hours and the implications on productivity in the public and private sectors. The latest fuel price increase, juxtaposed against issues of national cohesion, anger, poverty, and security, can only succeed in further deepening mass poverty and heating up the polity. It is quite certain that the cyclical hike in price of domestic pump price of fuel in Nigeria, which always culminates in nation-wide strikes, constitute enough disincentive to foreign investors than attracting them. This, in our view, is one, among some, of the inestimable costs imposed on the Nigerian economy and underscores a need for rigour in analyzing issues of public policy.

In view of the reflationary stance of the proposed 2005 budget, as a result of the settlement of domestic public sector payment arrears as provided for in the budget, in addition to higher public expenditure (with minimum 80% implementation), we again expect rising contribution of fiscal policy to economic growth over the coming year. In 2005, given expectations for slower global economic growth, and by extension, slower rate of growth in demand for oil, it is likely that oil prices will recede from their highs, whilst remaining above their historical levels. We do not expect much improvement in the contribution of industry to overall economic growth as long term issues of infrastructural deficiencies remain. In this regard, the spectre of ever rising non-oil imports, coupled with our expectation for slower growth in oil exports, suggests that net exports will prove less of a growth driver in 2005 than 2004. Following the large increases in oil and gas production in 2003-04, coupled with record high oil prices there has been significant increase in Nigeria's GDP base - thus creating a high hurdle rate for growth over coming years. Nevertheless, subsequent steady increases in oil and gas production should drive real GDP growth, even with only limited progress in economic reform. From the foregoing, we are somewhat skeptical of the government's ability to achieve the 6-7% target set in the proposed 2005 budget, believing that growth is likely to be slightly muted. **Thus we see 2005 GDP growth in the region of 4 - 5.5%.**

Recognizing the need for improved social sector spending, which we had mentioned in our July 2004 report, the 2005 budget proposal has made provision for

- a contributory pension scheme that will

assure new pensioners of a steady income in their old age;
- a new health insurance scheme that will assure workers in the public service of a good standard of life-long health care through qualified physicians, nurses and other medical personnel;
- increased support to the National Poverty Eradication Programme so as to support women and youth at the grassroots; and
- support for a new social assistance program targeted at the youth, women, and the elderly.

POLITICS AND REFORMS: IN WHOSE BEST INTERESTS?

Despite the firm grip of the president's People's Democratic Party on power, a climate of tension and uncertainty still prevails throughout the country, created by, perhaps, ongoing politically motivated violence. We expect the President to use political domination of the National Assembly to push ahead his administration's proposed programme of economic and political reform in the coming two years. The risks and challenges facing the government are formidable; consistent policy implementation will be essential to successful reform.

Whilst it is generally accepted that civilian rule in Nigeria has come to stay, we express concern regarding the country's political stability, particularly given the massive rewards that political power affords office bearers. Although the next elections are a couple of years away (due in 2007), political campaigning has already begun in earnest. President Obasanjo is not standing for presidency again unless the constitution is changed to allow for a third term of office; but this does not seem likely. With the most powerful job in the country up for grabs, the Nation is already in a state of high excitement, which began even before the President was inaugurated for his second term. All of these have implications for policy implementation, continuity and overall stability, which are all matters of concern to investors. As borne out by earlier reform efforts, the on-going reform programme is, however, likely to face considerable opposition from vested interests within the political elite and from the trade unions, which are deeply opposed to certain aspects of the reform agenda. In particular, we are of the opinion that emphasis on public service reforms, accountability and transparency will help establish key building blocks to strengthen institutions and facilitate the effective implementation of reforms that are resistant to reversal. The reform process could well grind to a halt in the second half of 2006 as political in-fighting increases before the 2007 elections. Commitment to further reform will then depend largely on who succeeds as President.

MANUFACTURING

Globalization, by linking up national economies, throws up tremendous opportunities and threats for business. By linking business to markets which were hitherto unknown to them, it provides access to new and larger markets and prospects for growth. It also provides access to more competitive sourcing of inputs, improves the availability of information, and creates opportunities for beneficial business partnerships with foreign businesses. Despite the opportunities, globalization has presented tremendous challenge to local manufacturers. The virtual elimination of the protection offered in national markets has increased competition from foreign products. Domestic customers, having also become more discerning by the exposure to quality products, are not prepared to settle for less. The diminishing effective market, posing a threat of survival for domestic manufacturers, informed the import prohibition policies of the current administration.

We restate our earlier view that government's efforts to address the perceived negative consequences of globalisation in the country, through import prohibition policies, may not yield the desired results, unless it first makes sure that the local industry is competitive enough. Protection of the domestic industry through high tariffs and import prohibition has thus generated a paradox - they have encouraged imports because the smugglers know that due to high demand for their goods, they can bring them in with paying only a fraction of the real duty. In so far as these measures have spun lucrative illegal importation, they in fact substantially undermine the goal of protection of domestic industry. Underscoring this, according to the Manufacturers Association of Nigeria, 55% of Nigeria's import figure as at December 2003, which translated to about $6.3bln or approximately N800bln, was lost to smuggling. It is, therefore, clear that the import substitution strategy that has long guided our industrialization efforts is inconsistent with the realities of a globalised world. Even where effective, the import substitution strategy promotes sub-optimality in the local industry.

The low levels of the share of manufacturing value - added in Gross Domestic Product, and the share of manufactured goods in exports, point to the fact that Nigeria is not yet industrialized. The government must position the industrial sector to take maximum advantage of the trade opportunities afforded by globalisation through capacity building and structural change. Effective re-positioning of the nation's industrial sector to meet the challenges of a globalised economy requires attaining competitiveness at both the level of the firm and that of the national economy. Trade polices should encourage external competitiveness rather than create a bias toward import substitution. For Nigeria to achieve rapid growth, there is the need to develop her exports by tapping into the global value chain. The nation can do this through building strong local capacities in domestic enterprises-the route taken by the Republic of Korea and Taiwan-or attracting export-oriented FDI-a strategy Malaysia employed in the early phase of its industrialisation journey. The critical factor in globalisation therefore, is competitiveness and this should be the thrust of our industrial policy.

The present administration has made some efforts in improving the state of infrastructure in the country - most notably the revolution in the telecommunication sector. The Government's focus on power and roads in the 2005 budget proposal is a step in the right direction, and is important for private sector development; a trend expected to be sustained through the medium term so that Nigeria can steadily make up for its infrastructure deficit. The government's aim is to double current power generation capacity within the next three years and to substantially rehabilitate, repair and maintain all Federal roads whilst completing those that are far advanced i.e. past the 70% completion point, particularly major arteries that are key for economic activity. Passage of the **Public-Private Partnership Bill** is imperative as it will be able to regulate public-private partnerships in infrastructure development and hopefully pave way for innovative private sector approaches to infrastructure provision. The resultant division of labour and specialization will result in improved efficiencies and product quality. At the state level, certain state governments have made progress on this front; for instance the Lagos State government, in November, passed the State Roads, Bridges and Highway Infrastructure (Private Sector Participation) Development Board Act.

Official figures released by NEPA show that more than $2bln have been expended on revamping operations of the authority. The deterioration in electricity supply has adversely impacted the manufacturing sector, largely due to the colossal cost incurred in running power generation sets due to NEPA's inefficiency and the deregulation of petroleum products prices. We agree with the World Bank's assessment that unstable power supply remains the bane of the manufacturing sector (energy costs are estimated at over 13% of final production costs). Going by the Federal Government estimates for on-going privatization proceeds in its 2005 budget proposal (N4bln), it appears that the government has again postponed the privatization of key state owned enterprises such as the Nigerian Telecommunications Limited, National Electric Power Authority (NEPA) and the Nigerian National Petroleum Corporation. Against this background then, we express concern regarding the government's ability to drive significant improvements in this sector, in view of considerable investments required in terms of capital and technical expertise to get steady electricity supply. Given the key role played by the power sector across the economy, we are of the opinion that the government should be more decisive about tackling the inefficiency and buck passing in NEPA, in addition to focusing on creating an enabling environment for the deregulation and liberalization of the power sector and be more decisive about tackling the inefficiencies of NEPA. It is against this background that a more drastic action needs to be taken; the absence of which would derail the key precepts of the Federal Government's NEEDS programme.

In line with reforming the regulatory framework for trade in Nigeria, which is essential to enhancing Nigeria's growth prospects, the Federal Government is working on measures aimed at simplifying tariffs and streamlining taxes by bringing greater clarity into import regimes. These reforms are expected to take effect in mid-2005 and all products, except banned items, are expected to be phased into this regime starting June 2005. In the 2005 budget proposal, the Federal Government also stated its intention to continue the use of additional tariffs to protect selected sectors where the country has comparative advantage. Banned products are expected to be phased into the new tariff band starting January 2007. We note that these import bans may be inconsistent with World Trade Organization rules and reiterate our concern over the government's use of import bans as an instrument of protection. Furthermore, the government has stated its intention to re-introduce the Export Expansion Grant[12] scheme, which was suspended since July 16, 2004, in the fourth quarter of 2004. The suspension was a necessary step aimed at ensuring that only genuine exporters benefited from the scheme following the exploitation of loopholes by beneficiaries and the administrators to perpetrate fraud. Our view is that manufacturing remains the best engine for economic growth, for the following reasons:

- It is less exposed-unlike crude oil-to external shocks, price fluctuation and unfair competition.
- It is the main vehicle for technology development.
- It drives and defuses innovation.
- It is a large employer of manpower, and
- It is the largest trainer of unskilled labour

PRIVATIZATION: TRANSPARENCY IS KEY

As at September 2004, the government had realized ₦5bln from the sale of government r properties in Lagos, and about ₦4.8bln from the privatization or divestment of Federal Government shares in West African Refinery, Sierra Leone, National Trucks Manufacturing Company, Peugeot Automobile of Nigeria, Delta Steel and Daily Times Corporation. The success of privatization depends very much on institutions of market economy such as legal frameworks that define property rights, private contracts, dispute resolution mechanisms and rules of entry and exit of business enterprises. The general impression remains that vested interests and political influences continue to interfere with the process; thus privatization needs to be carried out in a more transparent and fair manner. The importance of ensuring

[12] This fund provides cash inducement for exporters that have exported a minimum of N50,000 worth of semi-manufactured products. The cash incentive is to enable such exporters to (i) increase the volume and value of export; (ii) diversify their export products and market coverage. Since 1997, government approved a uniform rate of 4% of foreign exchange repatriated as basis for computation of export expansion grant. This fund is only available to exporters who have repatriated in full the proceeds from their export transaction. The repatriation must be certified by the CBN to be eligible.

transparency cannot be over-emphasised in an environment characterised by suspicion and distrust; it creates a general perception of a level playing field which helps to build support for the privatisation process. Initial policy reversals, following the change of government have affected the enthusiasm of some international organizations desirous of participating in the programme.

THE EXTERNAL SECTOR

Globally, due to better economic growth, increasing corporate profits, higher stock prices and more mergers and acquisitions, the outlook for foreign direct investments (FDI), both in the short- and medium-term, is promising. FDI is increasingly being targeted at services, especially the business, financial, telecommunications and leisure industries, and away from manufacturing and primary industries. In Africa, we see privatisation continuing to play a key role in the influx of FDI on the continent. Difficulties faced by prospective investors in Africa are transparency issues, the lack of a functional regulatory framework, political risks, macroeconomic instability, as well as frequent changes in economic policies or positions of government officials. In response to these concerns, African governments have made concerted effort to liberalise regulatory regimes, improve the business conditions for FDI, and actively promote investments. Despite these improvements, sub-Saharan Africa's (SSA) share of FDI in developing countries continues to decline, due in large part to the mediocre degree of reforms implemented compared with those in other developing countries. As a consequence, relative to other regions, SSA has become less attractive for FDI. Not suprisingly, for 2005, most Trans National Corporations expect FDI flows to remain steady in Africa[13]; South Africa and Nigeria were the only sub-Saharan countries among the top five destinations for the continent as a whole.

Historically, Nigeria's poor external image has substantially reduced the magnitude of foreign exchange inflows into the country, and continues to act as a disincentive to foreign investors. Given the slow pace of reform and the difficulty of implementation (caused in large part by an inefficient and bloated public service, but also by a lack of political will among politicians), the reform process appears ambitious. Nonetheless, we see improvements in this regard; to start with, Nigeria is making good progress towards sustainable economic growth, in part a result of its new economic reform programme and political stability. As a result of strengthened support for the Independent Corrupt Practices and Other Related Offences Commission, Economic and Financial Crimes Committee, and other national law enforcement and security agencies, the government expects the repatriation of close to $500mln by the government of Switzerland. In addition, Nigeria possesses a wealth of unexploited natural resources that include vast amounts of arable land, rich forests, relatively well-educated labour force, petroleum resources, natural gas, and other mineral resources. Good trade links with the rest of West Africa, providing access to a market force of 250mln thus make it a good target for foreign investment. With the successes achieved from the deregulation of the telecoms sector and on-going, albeit marginal improvements in infrastructure, coupled with the government's strong desire for accountability and transparency, Nigeria is set to become a competitive location for FDI.

ENERGY - BENEFITING FROM AN INCREASING CONTRIBUTION FROM NATURAL GAS

Below normal oil inventories across the industrialized countries has contributed to concerns about the adequacy of supply to meet rapidly expanding global oil demand. We believe that the structure of the crude oil market has changed in the last two years and is now favourable to structurally higher prices.

[13] UN Conference on Trade and Development

However, in 2005, global oil demand is expected to decelerate as high world oil prices begin to slow the pace of world economic growth. With regards to the gas sub-sector, between 2001 and 2025, global gas consumption is projected to increase by 67%, from 91trln cubic feet to 151trln cubic feet, representing 28% of the world's total energy consumption. Natural gas will continue to enjoy worldwide acceptance as a cleaner source of energy; accordingly, its share of the global energy-mix will progressively increase. This growing world demand for natural gas has enormous potential for the Nigerian economy - in terms of new jobs, stimulating industrial growth by developing the domestic gas market, capturing the economic value of gas through expansion of gas export projects, environmental gains, greater regional cooperation, new trading opportunities and relationships with the rest of the world. Consequently, government is currently focusing on a number of schemes, for monetising and utilizing large volumes of natural gas. These include: - Nigeria LNG, Brass LNG project, Nnwadoro floating LNG, pressurized LNG (PLNG), Gas-To-Liquid projects, West African Gas Pipeline, Trans Sahara Gas Pipeline, the Escravos Gas Project (EGP), etc. In order to provide a suitable environment for the considerable investments required in gas processing and utilization projects, the Federal Government has reviewed existing legislation to create a mutually beneficial legislative and fiscal environment that would fulfill government aspirations as well as ensure private investors a fair return on their investments. Longer term, while oil's contribution will not decline in the near future, it is expected that gas will be developed to a stage where its contribution approaches that of oil. Again, we see the short-term outlook for the external current account being dominated by developments in the oil sector and fiscal policy implementation.
Consequently, we see the current account moving into a deficit in 2005 as the price of oil falls back and imports remain high.

FOREIGN EXCHANGE MARKET: HOW LONG CAN THE NAIRA REMAIN STABLE?

We are maintaining our view that the near term value of the Naira will be determined mainly by the balance of trade regardless of relative dollar strength and will be directed primarily by the oil price movements and oil revenue accruing to the government. Thus, with oil prices set to remain over US$30/barrel in 2005, the outlook for the Naira in 2005 appears positive. The CBN is likely to continue to intervene in the currency market to support the Naira on the back of strong foreign exchange inflows. This remains our view in spite of our expectations that demand at the Dutch Auction System will remain high. In real terms however, the Naira has actually depreciated substantially against major currencies; since the underlying issue is not really one of Naira stability but global US dollar weakness. In addition, the adoption of the fiscal rule of saving excess revenue above the proposed $27 per barrel on which the budget is based, to smoothen out revenue disbursement, will help stabilize the volatility in the money market. We feel that the Naira can continue to maintain its present level against the dollar, with a good chance of modest appreciation, more so with continued declines in the value of the US dollar. We forecast a trading range for the Naira of ₦136/US$1 and ₦145/US$ in 2005.

HIGH AND RISING DOMESTIC FUEL PRICES: AN ECONOMIC ALBATROSS

Despite being Africa's largest oil producer, with four state-owned refineries with a maximum daily capacity of nearly 440,000 barrels, operations within the downstream sector have remained problematic. This is a consequence of the Nigerian National Petroleum Commission's (NNPC) monopoly of refining and inability to maintain the country's four refineries; with the ultimate effect of grossly inadequate supply of petrol, diesel, and kerosene nationwide. In spite of colossal sums spent on turnaround maintenance, refining output has remained at low levels, with the result that Nigeria imports about 70% of its domestic fuel requirements. So far, the NNPC has anchored the argument for the fuel price increase on rising crude oil prices in the international market. From the foregoing however, given expectations that crude oil prices for the rest of the year and 2005 are likely to remain above their historical levels, we are concerned about the government's predication of deregulation entirely on market forces. In the absence of functional refineries able to service domestic demand, it raises the spectre of ever rising domestic fuel prices; with the attendant detrimental effect across all spheres of economic activity.

In a bid to create strong and competitive energy markets that will ensure Nigeria has secure, diverse and sustainable supplies of energy at competitive prices, the authorities have formulated an ambitious strategy to privatize the downstream petroleum sector. This includes the sale of refineries, pipelines, and storage depots to strategic investors; and the opening of the sector to private investors in pipelines and other infrastructure. Following many years of neglect, the refineries require substantial upgrading, and recent experience with labour unrest may make workforce downsizing a difficult prospect - making these refineries unattractive to private investors. Consequently, the main challenge is to attract private investors to the refineries, and private importers to the products market. Investors are unlikely to come forward before the final regulatory regime for the sector has been specified. The current market structure is dominated by the NNPC infrastructure, with private marketers dependent on NNPC pipelines and storage facilities.

FISCAL POLICY: SUSTAINING FISCAL RESTRAINT REMAINS KEY

The main challenges in 2005 will be to restore macroeconomic stability, particularly with regards to inflation, continue the generation of savings from the oil windfall to protect against future oil price declines, and enhance the transparency and predictability of macroeconomic policies. Timely passage of the Fiscal Responsibility Bill would provide the legal underpinning for prudent consolidated fiscal policy at all levels of government over the medium term. We maintain that the primary risk to effective macroeconomic management continues to be the pro-cyclical stance of fiscal policies at the sub national level and increasing availability of more funds to State Governments. In 2005, in view of the plan to spend 50% of excess oil revenues in the coming year, there is a need for the continuation and reinforcement of recent fiscal tightening at the federal level, accompanied by appropriately tight monetary policy.

DEBT

Nigeria's external debt presently stands at $34bln, up from $32.9bln as at December 2003. The $1.1bln increase in debt stock was partly due to adverse exchange rate movements of the dollar vis-à-vis European currencies in which a large part of the debt is held and partly due to arrears accumulation. The Federal Government intends to seek the understanding of the Paris Club on lower debt service payments based on significant needs for infrastructure expenditure. Total domestic debt stands at N1.329trln, most of it in short term treasury bills as a result of the Federal Government use of a mixture of market-based and monetary financing to fund its expansionary policies over the years. The Debt Management Office (DMO) has put stringent conditions against further reckless external borrowings by government at all levels to avoid worsening the situation. In line with the West African Monetary Zone convergence criteria, the Federal Government's borrowing will be reduced in 2005; as part of the criteria for the eventual emergence of a single monetary zone in West Africa, governments within the region are compelled to restrict their borrowing from Central Banks to not more than 10% of the previous year's retained revenue. Currently the Federal Government can borrow up to 12.5% of the pervious year's retained revenue from the Central Bank of Nigeria.

With over 60% of the domestic debt concentrated in three-month instruments, the government is exposed to high rollover and interest rate risks. An immediate priority then, is the need to lengthen the maturity profile of domestic debt, and ensure a more even distribution to address the bunching problem. The DMO states that the restructuring of the Nigerian Treasury Bills into longer tenures will gradually phase out treasury bills in the management of the country's debt within the next three years. We note, however, that in the absence of credible fiscal and monetary policies, investments in longer-dated instruments would likely come at a high cost. Longer term, as macroeconomic stability takes root, the government's borrowing cost should decline, permitting the sustainable development of the government bond market. Overall, we anticipate that the domestic debt management reforms would strengthen liquidity management - through the formal separation of monetary and debt management operations - exert market pressure for fiscal discipline, improve oversight over public debt management, and spur capital market development.

INFLATION IS LIKELY TO TREND LOWER

To achieve price stability and exchange rate control, there is need for the removal of sources of surplus liquidity and other distortions within the system. With a considerable amount of the currency in circulation being outside the banking system and, consequently, outside the control of the CBN, liquidity forecasting has been very difficult. The recent fuel price hike[14], and uncertainty regarding the future direction of crude prices (both global and domestic), coupled with the spectre of increased government spending over the coming year as stipulated in the 2005 budget proposal raise concern regarding the attainment of the Federal Government's target inflation rate of not more than 10% in 2005. To start with, the fuel price hike has already led to an escalation in the prices of goods and services. With product prices being fully flexible over the long term, we expect that prices will catch up with higher input costs, ultimately fuelling higher inflation and leaving the CBN with no recourse for controlling inflation and inflation expectations. Given the government's intention to continue the import ban over the coming year, we also anticipate the sustenance of high prices on such contraband goods. Our sense remains that in order to enhance the effectiveness of monetary policy there is a need to address the issue of over reliance on fiscal policy. Consequently, while we see a moderation in the rate of inflation, we view as far fetched the optimism of the Monetary Policy Committee[15] of the CBN of achieving a single digit inflation rate by the end of the year 2004 as expressed in its September report. Having said this, positive drivers with regard to inflationary prospects are

- Successful fiscal restraint which has led to the government's undershooting its money supply targets in the year to September 2004;
- the CBN's ability to resort to Open Market Operations, the adjustment of key bank ratios (cash reserve and liquidity), discount window operations, or duration substitution of government securities in a bid to control liquidity;
- the government's intention to increase external reserves to $15bln in 2005, implying a conscious effort to reduce the amount of currency in circulation; we note, however, that given the current level of external reserves, ($14.7bln) there might be an upward review of this target;

[14] The Nigerian National Petroleum Corporation increased the prices of petroleum products by 26% (from ₦43.90 to between 51 - 54) on the 26th of September this year.
[15] The committee expects that the combined effect of the high international oil price and a continuation of current prudent macroeconomic policies would help to lower the inflation rate close to single digit level by the end of the year.

- favourable year-on-year comparisons as one-off effects of the fuel price hike drop out of the calculation;
- the adoption of the fiscal rule;
- the effect of the pension legislation, and;
- the expectation that the stated deficit of N314bln in the proposed 2005 budget, will be financed through non-inflationary means.

Downside risks to achieving the inflation target are
- that inflation expectations may be deeply entrenched given the weak track record on macroeconomic stability;
- the component of the price index that may be directly affected by monetary policy is relatively small given the large share of food (30%) in the price index;
- the CBN, through political pressures to keep interest rates low, may lack independence to pursue a more aggressive disinflation objective if required; and
- the possibility of even higher fuel prices.

We have concerns regarding the government's intention of funding about N70bln (22.29%) of the N314bln budget deficit with long term funds to be raised from the capital market. Just as we said in our July report, the search for long term funds in the capital market for funding the deficit in the 2005 appropriation bill is a step in the right direction. However, the N25bln capitalization requirement for banks has led to a wave of fund raising activities within the sector; suggesting the possibility for under subscription of the Federal Government's bond issue. To the extent that banks constitute the largest subscribers to the federal government's issues, the possibility of a not being able to successfully access the capital market is very high. This, then, raises the probability of reversion to the traditional Ways and Means mode of financing the deficit funding and building up of inflationary pressures within the economy.

On balance, we expect that inflation will decline in 2005. **Our 2005 forecast range for consumer price inflation as measured by the 12-month moving average is 10 - 16%.**

INTEREST RATES: FINALLY HEADING SOUTH OF THEIR OWN VOLITION

The conduct of monetary policy will be critical to supporting a disinflation strategy. The shallow financial market complicates CBN's conduct of monetary policy as more forceful use of liquidity management to pursue price stability would adversely affect government's debts servicing costs. We are of the opinion that reforms should also be considered to strengthen the CBN's independence and further enhance the soundness and stability of the banking system. The CBN, together with Nigeria Deposit Insurance Corporation, should continue to strengthen governance practices in the banking system, adopt zero tolerance for misreporting and violation of existing prudential regulations, and design a viable exit strategy for weak banks. This is because enhanced financial strength will be critical to improving the transmission channels of monetary policy and achieving the authorities' growth objectives. In view of the huge funds inflow into the banking system following the CBN's reform agenda, in addition to the spending of some of the excess oil revenues over the coming year, we expect an overall decline in interest rates. This remains our view even in the event of limited sterilization through the CBN's resumption of the withdrawal of public sector funds from the banking system. Even if fiscal policy were to loosen significantly, we see it being politically difficult for monetary authorities to raise the Minimum Rediscount Rate as this could be detrimental to NEEDS' objective of higher economic growth. Thus, we see monetary policy authorities favouring corrective fiscal measures, in addition to direct controls such as raising the cash reserve requirement and/or shifting of deposits of nonfinancial public enterprises from commercial banks to the CBN as well as allowing for higher accumulation of net international reserves.

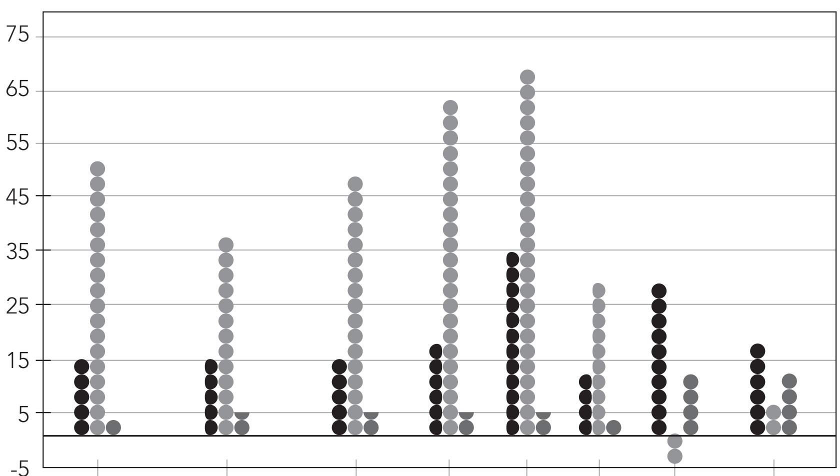
EQUITY MARKET: OUTLOOK RATHER CLOUDY

We see the ₦25bln capitalization requirement by the CBN continuing to drive activity in the equity market over the first half of the coming year as companies, especially operators within the banking sector, raise fresh capital. Longer term, we see the integration of structures and processes within the banking industry as the biggest challenge confronting companies in the merger and acquisition arrangements. Key integration areas are staff, information technology, and banking operations. Thus, to an extent, we expect that the uncertainty generated by the banking reforms will remain within equity markets for some time to come. Furthermore, post consolidation, we see a resurgence in speculative activity in the equity market as banks resume margin lending and direct equity market participation in a bid to improve returns on capital. Given the much higher capital base of surviving banks, we see this having a more significant impact on the market than previously obtained. In our July 2004 report, we had dwelt extensively on the positive impact of on-going pension reforms[16] on the Nigerian equity market; the new pension bill has mandated the creation of the National Pension Commission, which will regulate the management of pension schemes and private sector pension fund managers. Given the country's history of pension savings being eroded through mismanagement, and more often corruption, the new law augurs well for greater transparency and more prudent investment of pension savings - a positive stimulus for capital market development.

Rising operational expenses and higher product prices due to the recent hike in oil prices will lead to rising operational costs for companies, and by extension, reduced profitability. The only major gainers from the new fuel price are likely to be the oil majors, through rising profit margins. Rising inflation, coupled with higher costs of consumer goods may lead consumers to either reduce volumes purchased, or alternatively, their budgets to accommodate the same quantity. However, since most consumers would find

FIGURE 6: Relative valuation of the Nigerian All Share Index to other Emerging Markets

Source: Merrill Lynch Emerging Market Weekly Update (Nov. 29th, 2004), ARM Estimates



	Emerging Asia	EM Europe & S. Africa	Latin America	South Africa	Chile	China	NSE	NSE ex aberrations
● PE (times)	15.1	14.6	14.9	19.7	35.3	12.8	29.69	16.8
● Earnings Growth (%)	51	37.9	48.3	64.2	72.1	30.8	- 4.39	3.77
● Price to Book Ratio	0.3	1.7	2.3	2.8	1.8	1.7	11.77	14.48

it difficult to increase their budgets in the face of limited income, we sense that the most likely scenario will be a cut in the volume of demand; leading to a drop in sales volumes and shrinking profit margins. Furthermore, customers are being more demanding and less loyal, and forcing companies to be more innovative, albeit at further cost. On going pension reforms constitute another risk factor to corporate profits as companies might be forced to fund pensions deficits which may be significant. For example, Nigerian Breweries and Guiness, in 2001 and 2002, voluntarily funded shortfalls in acturial valuations of their gratuity scheme liabilities to the tune of about N1.8bln and N1.2bln respectively. More recently, UACN Nigeria Plc, after providing N298mln for its pension deficit in 2003, has stated its intention to provide for the balance of N806mln over a five year period. However, a supporting factor for corporate profits over the coming year is our expectation for lower interest rates and by implication, reduced interest burden, thus mitigating some of the downward pressure on corporate profits. We will continue to monitor interim results, laying emphasis on companies able to exhibit better cost control relative to their peers in the current environment.

We remain convinced of the importance of equity valuations i.e. the level at which the marketplace is pricing the current earnings power of publicly traded

Table 5: Valuation Parameters for the Nigerian Equity Market

Industry Group	Div Yld[a]	Current P/E[b]	P/E Est[c]	YTD Perf[d]	Price to Book[e]	Price to Sales[f]
Banking	3.64%	10.25	8.99	12.19%	2.91	2.10
Brewery	4.85%	54.6	40.48	34.14%	9.2	4.53
Building Materials	1.52%	4.24	7.63	19.02%	4.85	0.74
Conglomerates	4.96%	17.52	17.83	31.05%	6.96	0.43
Food & Beverages	3.63%	21.91	20.32	24.07%	23.62	0.83
Petroleum Marketing	3.29%	22.49	18.16	42.52%	15.07	0.18
Property	6.82%	14.15	11.8	40.20%	0.63	2.56
Market Average*	4.02%	29.69	23.69	13.57%	11.77	2.71
Market Average (ex aberrations)**	4.78%	16.80	14.96	28.18%	10.68	1.98

a) based on most recent full year dividend and price as at 30th November 2004
b) based on 12-month trailing earnings per share
c) based on full year earnings estimates for fiscal 2004
d) performance as at 30th November 2004
e) based on most recent book value per share
f) based on 12-months trailing sales per share
* Represents 71% by Market Capitalization of the Nigerian All Share Index; all ratios are market cap weighted
** ex Nigerian Breweries, Oando Plc and Mobil Plc
Source: ARM Estimates

[16] Under a contributory pension scheme, public sector employees are obliged to contribute 7.5% of their salary while the government contributes 10%. In the private sector, employer and employee can agree on any ratio that amounts to no less than 15% of the employee's salary.

corporations, over the long-term. While earnings, ultimately, should drive long-term share prices, investor psychology drives short-term fluctuations in stock prices; sometimes contrary to what the state of valuations suggest ought to happen. For the Nigerian equity market, whilst valuations are more attractive than obtained at the end of the first half of the year, at a P/E ratio of 16.8 times its average 12-month trailing EPS (table 5), the Nigerian equity market appears expensive relative to other regions (see fig 7). In our view, this is attributable to much lower profit growth (see fig 7) as a result of the dearth of infrastructure, the deregulation of petroleum prices, policy inconsistencies, weak regulatory and generally difficult operating environment for businesses in Nigeria.

For instance, average cumulative earnings of Nigerian companies as at half year 2004 declined 4.39%, relative to a 22.22% rate achieved over the same period in 2003. In trying to decipher the true growth in earnings achieved, we have stripped the index of sharp aberrations in growth rates recorded over the first six months of the year. These were a 59% decline in after tax profits for Nigerian Breweries, which remains the most capitalized stock on the NSE All Share Index, coupled with a 262% and 138% growth in earnings for Mobil and Oando Plc. Stripped of these aberrations, average earnings grew a paltry 3.77% in H1'04 relative to 20.88% as at H1'03.

In the short term, given our expectations for reduced growth in profitability, there remains the possibility of valuations deteriorating from current levels. Medium to longer term however, given the Federal Government's economic reform programme, coupled with the focus on implementing a public-private partnership, which should drive operating expenses lower, and therefore boost overall corporate profitability, we see valuations improving considerably. Government policy reforms which hold significant promise for improved equity market performance over the medium to long term are

- the power sector reform bill expected to spawn an era of more efficient production and distribution of electric power;
- the banking sector reform which we expect to decrease borrowing costs and improve investment climate, and;
- the pension reform bill, and ensuing availability of fresh/long term funds into the capital market

Over the past few years, reflecting the global phenomenon, there has been a decline in the dividend yield on Nigerian equities; largely attributable to significant price appreciation, and to a lesser extent, lower dividend payout. Our estimate for the 2004 dividend yield (table 5) for the Nigerian equity market is about 4.78%, down from 5.52% and 6.81% as at 2002 and 2003, respectively. Average dividend payout ratios have been lower because corporate managers have retained and reinvested a greater share of earnings. Given the mediocre growth in nominal earnings per share (H1'04: 3.77%), it might appear, first hand, that these retained earnings have not been relatively well invested as the decline in the dividend yield has not been compensated by strong earnings growth. We hesitate to come to that conclusion however, given significant capital expenditure for capacity expansions and plant upgrades that have taken place in Nigerian companies over the past 6 - 24 months, and which as yet, have not fully reflected in companies' bottom lines.

Historically, dividend and bonus announcements provide significant technical support to the equity market - particularly over the first half of the year given the predominance of companies with December year-ends. Over the coming year however, we expect much lower support from this as a result of the following

- a significant number of companies declared bonuses over the past year, and are not likely to do so over the coming year
- fresh capital was raised across different sectors of the equity market, resulting in a considerably higher number of shares outstanding and attendant serviceability issues with regards to dividend payments
- resultant dilution in per share matrices in the short term due to fresh capital injection
- lower growth rates in profits and therefore, a probable decline in the growth rate of expected dividends

On the other hand, we see lower interest rates on money market instruments providing support to equity prices in terms of improving liquidity as investors reallocate assets from the money market to the equity market. Overall, whilst the macro-economic landscape appears positive for the equity market, we express concern regarding the technical factors, which traditionally, have greater impact on equity returns. Across sectors, in the current environment, combining relatively attractive valuations with potential for earnings growth, the **petroleum marketing, banking**, **breweries**, and to a lesser extent, the **building materials** sector rank highest (table 5). Our stock picks are **Guinness, First Bank, Union Bank, Afribank, Oando Plc, Ashaka, Total, Conoil, UACN Nigeria, Nestle Nigeria Plc, Zenith International Bank Plc, and Guaranty Trust Bank. For H1 2005, our recommended asset allocation for a typical growth portfolio is 70% Equities and 30% Fixed Income.**

The development of a nation's capital market provides opportunities for greater funds mobilization and improved efficiency in resource allocation. Most developing countries have relatively young and weak market-based financial institutions such as stock markets. For emerging markets, trade openness and high quality of accounting standards are conducive to the development of local equity markets. Developed countries with greater economic freedom and stronger shareholder protections are associated with increased market capitalization. Whereas issues such as insider trading, and behavioral responses are applicable to stock markets all over the world, the prevalence of strategic manipulation of prices is of particular importance in emerging markets and is applicable to Nigeria. As a result of weak regulatory and contractual enforcement in emerging markets, which result in poor corporate governance of firms, foreign investors are deterred from local equity markets for fear of being exploited by unscrupulous stock price manipulators; because manipulation of prices is more likely to occur in newer and shallower markets.

In a bid to continually improve the structure and dynamics of the equity market, authorities of the Nigerian Stock Exchange (NSE) raised the minimum number of units before which prices can be moved from 5,000 units to 15,000 units; this, in our view, should help reduce the level of speculative activity in the market. Other measures to improve the structure of the exchange are the trade alerts to further enthrone transparency, and a new settlement cycle, called NSE/CSCS settlement process, which will stop failed trades - a situation where stock brokers with unfunded accounts transact business on behalf of their clients. The NSE's initiative to automate its trading, clearing and settlement systems has improved market transparency and engendered investors' confidence. In addition, the constitution of a Joint Monitoring Committee has worked to accelerate the resolution of disputes and promotion of fair play.

For emerging market countries, financial liberalization, privatization and high quality of accounting standards are found to be associated with more efficient valuation. As an emerging market, Nigeria, in addition to meeting the long-term financing needs of the larger economy, faces significant challenges in establishing international acceptance. The NSE is working hard on various fronts to put it on the international scene. The NSE intends to co-operate with local and international capital market authorities, including partnering with its members to regulate the market in the desired direction. The upsurge in activity on the Nigerian equity market over the past couple of years is in part attributable to foreign portfolio investors, who increasingly see the market as combining security of investment with internationally competitive returns. Rising fixed investments by Guinness and Heineken in the brewery sector demonstrate rising confidence duly noted by portfolio investors. The NSE has been instrumental in working with the Ministry of Finance in preparing the country to receive a sovereign credit rating from an international rating agency. A sovereign rating would provide investors with a country risk guide. This should benefit the bond market in particular; allowing for issues to be priced relative to international benchmarks. With a credible price guide, investors, particularly foreign investors, would be able to invest with more confidence. Other incentives to stimulate development of the capital market are government guarantees for some instruments, such as mortgage-backed securities and favourable tax treatment for investors. Other policy recommendations include:

- developing the capital market to absorb the likely increased demand for investible funds
- full integration of the financial market (both the money and capital markets) to improve the effectiveness of interest rate policy and financial market liberalization

SECTOR HIGHLIGHTS

BREWERY

The Nigerian brewery industry has performed strongly in the last few years compared to its consumer product-manufacturing peers, benefiting from economic growth and improved consumer purchasing power.

Sector specific initiatives that have facilitated growth within the sector include:

- Capacity investments to increase supply capabilities;
- Increased marketing activity; and
- Supply chain improvements, reducing inefficiencies between production and delivery.

Cost-push inflation has however been a recurring issue for the sector, especially with recent hikes in fuel prices adding to the cost of production and increasing the rate of inflation. Other issues of concern include the poor state of infrastructure, particularly roads and electricity, and the high cost of finance (especially debt finance) for purposes of expansion. The trend in brewery strategy and operations evident from industry participants within Nigeria remains in line with their Global counterparts, focusing initially on intra-regional consolidation, with subsequent focus on organic growth and superior returns by reinvesting savings from cost efficiencies behind premium brands using intensive marketing initiatives. Nigerian Breweries Plc (NBL) for instance opened its new Ama Brewery in October 2003, in order to drive increasing sales and development of an enhanced brand development platform to cater for increased volume capabilities. NBL's main competitor, Guinness Nigeria, is also commissioning its Aba brewery in May, 2005.

On the equity markets, the Brewery sector[18] significantly outperformed the NSE - returning 34.14% in the year to November 2004, compared to the 15.61% return posted by the broader market (H1 performance for the brewery sector was 105%, while H2 performance was -29.96%). This reflects to a large extent technical support following Nigerian Breweries' 1 for 1 bonus in the first half of 2004, positive investor sentiment toward the growth potential within the brewery industry as well as the relatively

[18] Composed of Guiness and Nigerian Breweries

large capitalisation of the industry participants. In our view, valuations for Nigerian Breweries Plc are currently extreme, with the current PE of 97.91x relative to its closest rival, Guinness Nigeria, of 15.68x. We maintain our expectations in the short to medium term for depressed earnings and cashflows for the company as a result of its highly leveraged balanced sheet, and by extension, inordinately high interest payments, in addition to its increased working capital requirements. Given virtually zero probability of a 2004 bonus announcement from Nigerian Breweries over the coming year, we expect a shift in the market's focus to the magnitude of expected dividend payments. However, its huge amount of shares outstanding, 7.558bln, in addition to its currently depressed profitability, suggest the company might not be able to substantially increase dividend payments. Whilst we appreciate the fact that Nigerian Breweries is a significant component of the NSE index, and has grown its supply capabilities significantly with the introduction of the Ama brewery in Enugu, we remain of the opinion that the valuation concerns raised above and large debt burden, make a compelling case for an underweight allocation over the coming year. Consequently, both from a fundamental and technical perspective, we expect downward pressure on its share price. We maintain our **short term** recommendation of a **sell** which improves to **accumulate** in the **medium** term. Our only pick within this sector is **Guinness** based on its attractive valuations, strong earnings capacity and high dividend yield.

PETROLEUM MARKETING[19]

The global petroleum refining and marketing industry remains highly volatile and subject to significant changes in profitability and performance driven by economic and market trends. Refining over-capacity and increased market penetration of non-oil retailers has led to companies in the downstream industry struggling to achieve real growth in shareholder value. In addition, shifting demand patterns outside the US & Europe, and increasing focus on alternate fuel technologies are hampering the growth of the industry. The Nigerian downstream (refining and marketing) oil industry promises to be one of the most attractive growth markets in the world in the coming decades. Despite some level of improvement in the downstream in the last four years, many of the knotty problems of the industry still remain; prominent among these are the fact that the refineries are still not being operated as business units and are characterised by high-energy consumption, heavy budget maintenance, use of obsolete technology, and low capacity utilisation. More importantly, the supply and distribution network of the country also has its inherent problems among which are non cost recovery in all segments, continued NNPC monopoly, adulteration, hoarding, diversion etc. The Government's main objective for the downstream oil sector is to create strong and competitive energy markets that will ensure Nigeria has secure, diverse and sustainable supplies of energy at competitive prices.

The petroleum marketing sector remains a low margin business (see table 6); in view of recently released interim results, we reiterate our concern of shrinking margins within the petroleum marketing sector despite strong growth in turnover. Over the first half of 2004[20], average turnover growth for the petroleum marketing sector was 66.68% relative to a10.62% growth in profit after tax for the same period. We anticipate that the September hike in domestic fuel prices should lead to improving margins for the petroleum marketing sector, albeit, marginal. Over the year, the petroleum marketing sector outperformed the broader market, returning 42.52%[21] compared to the 15.61% return on the NSE. The sector, trading on an earnings multiple of 22.49x, is at a pre-

[19] Sector composed of Oando, Mobil, Total, Conoil and Texaco

[20] We have excluded Mobil and Oando from this computation as a result of the 262% and 138% rise in profits respectively which would have skewed the average significantly

[21] ARM Estimates

Table 6: Margins within the Petroleum Marketing Sector

	2003 Ind. Av.	Mobil	Oando	Total	Texaco	Conoil
Gross Margin	15.20%	17.96%	11.73%	13.74%	13.20%	19.36%
Operating Margin	5.64%	6.99%	3.98%	5.55%	5.26%	6.42%
Pretax Margins	5.69%	5.83%	1.59%	6.47%	5.76%	8.79%
Profit Margin	3.77%	3.93%	1.25%	4.02%	3.76%	5.88%

Source: Company Data, ARM estimates

mium to the market average of 16.8x. Our top picks within this sector are Oando, Total and Conoil. Within the context of our energy sector allocation, Oando remains, in our view, a core holding for investors, offering medium-term potential for delivery of top-quartile profitability and earnings growth characteristics versus sector peers. Relative valuation multiples offer the scope, in our view, for considerable out performance versus the industry.

Given the low margin business of the petroleum marketing sector, we remain biased towards market leaders such as Total, able to move volumes and benefit from economies of scale, in addition to its strong balance sheet and high dividend payout ratios. We have included **Conoil** as a further diversification play within the sub-sector as a result of its above average profit margins and relatively attractive valuations.

CONGLOMERATES[22]

In 2004, conglomerates continued to benefit from the Government's importation ban on several goods (especially consumer products) which forced consumers to turn to companies in this sector, majority of which engage in the production of locally manufactured consumer products. However, they were also faced with an increase in the level of competition as major players vied for a higher stake in the larger market. These impacted consumers positively, as the companies were forced to become innovative and improve the quality of their products in order to encourage brand loyalty and stronger demand. The Nigerian economy continues to offer strong growth potential to conglomerates in light of the high population density, rising personal income level, and potentially significant increases in per capita consumption levels in the country. However, the recent increases in energy costs constitutes a near term threat to the sector (as to all manufacturers) as higher production costs will put downward pressure on earnings, with companies not being unable to completely pass off higher costs to consumers. Consequently, to remain competitive, we expect conglomerates to become more innovative, offering consumers improved or wider array of products in order to induce higher demand.

Thus far, only UACN and PZ have reported half year 2004 results. Half year turnover growth for UACN was 12%; lower than its three year average half year growth of 24%; however, earnings grew 90% from H1'03 compared to its 80% three year average. Over the same period, turnover for PZ grew 19.27% compared to a 16.48% three year average; while earnings rose 7% compared to the firm's 29.42% three year historical average. Overall, earnings growth in the sector over H1'04 was 22.54%, compared to average earnings growth of 3.77[23]% for the broader market. On the NSE, the conglomerates sector returned 31.05% over the year, compared to the 15.61% return on the All Share index over the

[22] Sector made up of UACN, PZ, Unilever and CFAO
[23] Excluding Nigerian Breweries Plc., Oando and Mobil

same period. The sector appears slightly overvalued relative to the market; trading at a current PE of 17.52x and prospective PE of 17.83X, relative to a current and prospective Market PE of 16.8x and 14.96x respectively.

Notwithstanding, strategic initiatives undertaken by a number of companies within the sector, notably UACN and Unilever, in order to improve performance, bode well for higher earnings in the sector in the coming year. **UAC of Nigeria Plc**, due to its significantly attractive valuation and growth prospects, remains our top pick within the sector.

Since the inception of its restructuring effort in 1999, UACN's financial performance has shown gradual improvement. However, the heavy debt burden which the company carried from previous periods, and the resulting significant high interest rate payments, have kept significant profit growth in the company muted. In order to pay down its debt and fund growth plans, UACN embarked on a company recapitalisation exercise via an Offer by way of Rights to existing shareholders of 227,158,614 ordinary shares of 50 kobo each, at N12.50 per share in the proportion of 1 new ordinary share for every 4 ordinary shares held as at 4th June, 2004.

Over the next two years, **UACN** aims to reduce its significant debt burden in order to strengthen its balance sheet and enhance profitability. To improve revenues, the company intends to consolidate the dominant position of the Mr Bigg's brand by increasing its number of outlets to 247 by 2006 and will expand existing facilities in MDS, its outbound logistics division. More importantly, it plans to expand its revenue lines by expanding into the premium segment of the Quick Service Restaurant market via the Innscor franchise brands which comprise Nandos, Chicken Inn, Creamy Inn, Pizza Inn, Dial-A-Delivery and Inn-The-Jungle. The brands were secured through a strategic alliance with Innscor International and Mobil Oil Nigeria PLC.

We view the following as areas of strength for the Group:

- The quality of its current management which has proven its strategy formulation and execution capability over the past five years. We are fairly confident that if the current dedication to strategy execution is maintained, the company will return to full capacity and profitability in the medium-term.
- Its expanding distribution network which offers it wide coverage and access to a large market share particularly in its food business
- A lengthy market presence, which has helped the company to establish a strong brand name and economies of scale across various business sectors.

We are encouraged by the company's recapitalisation initiative which will improve its cashflow position, provide funds for partial repayment of its debt and offer capital to fund the company's long-term expansion plans. UACN appears committed to rebuilding its marketing culture in order to deliver superior customer service and innovative products that meet consumer needs. Consequently, we expect positive consumer response, ultimately resulting in higher demand for the company's products. This should favourably impact sales and revenue for the company in coming periods.

Unilever Nigeria Plc, due to its recent repositioning, represents more of a diversification play within the sector as a whole. The company has reduced the number of its manufacturing facilities through consolidation of existing factories, reduced the number of its brands in order to cut down on costs and boost profitability, and overhauled its supply chain via truncation of its production and distribution processes. Proceeds from the sale of its old factories have been used as an inexpensive means of funding its expansion plans. Unilever has embarked on an expansion strategy; the company has focused on aggressively marketing its leading brands with emphasis on increasing distribution and availability throughout the country, especially in the rural areas which currently forms an untapped source of revenue in the consumer goods industry. To this end, Unilever is significantly increasing levels of investment in advertising and marketing support for its leading brands and broadening its distribution network into the rural areas in a bid to penetrate the market.

Another factor that underscores our positive view on the company is its placement by Unilever Oversees at the centre of its expansion plan in the ECOWAS region. This should substantially increase Unilever's market size as the company becomes the base from which products are manufactured and sold to all countries in the ECOWAS region. With regard to production costs, the organisation stands to benefit from aligning its development processes with other Unilever subsidiaries in West Africa. This should enable it to leverage on the economies of scale associated with a regional and global supply chain process in terms of sourcing cheaper raw materials from its counterparts in the ECOWAS region and ready distribution channels in West Africa. We expect the above to significantly improve the company's market size and its revenues over the medium- to long-term.

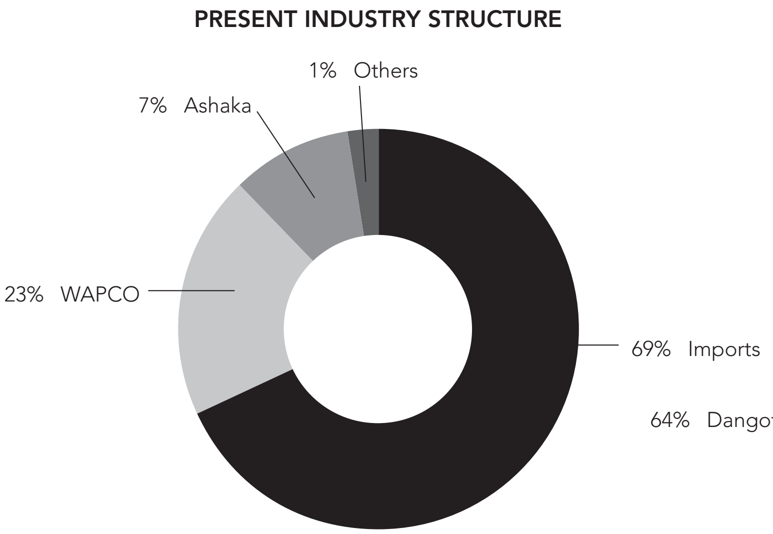
BUILDING MATERIALS[24]

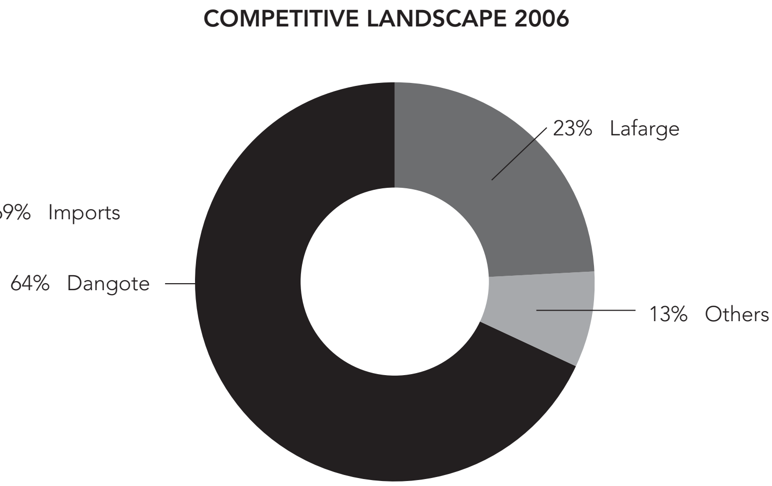
The competitive landscape in the Nigerian cement industry is changing. New entrants into the cement manufacturing sector and the rehabilitation of many of the existing but moribund plants are creating a shift from import competition to competition within the local market. Thus the supply of cement in the country is experiencing a change from domination by imports to increasing preponderance of local content in terms of manufactured outputs. Furthermore, once dominant local manufacturers may have their status challenged by aggressive new entries. Notably, we expect WAPCO, which previously held the largest share of manufactured cement among the local manufacturers, to have its primacy usurped by Dangote Group, which is in the process of building new cement plants across the country and revamping those it has acquired. Some of the emerging changes include:

- The upgrade and expansion of the Benue Cement Company's plant in Gboko, Benue State by Dangote Group, to 3.0mln tonnes p.a., from the current installed capacity of about 1 Mt p.a..
- The construction of a new 3.6 Mt p.a. cement plant in Obadjana, Kogi State, which is expected to be the largest in sub-Saharan Africa when it comes on stream in 2005; and a new 1.8 Mt p.a. Ibese, Ogun State, also by Dangote Group.
- The renovation of 500,000 tonnes p.a. plant of the Bendel Cement Company, in Okpella, Edo State by Scancem and also, the revitalisation of the 250,000 Mt p.a. Calabar Cement plant.

The charts on the next page show the competitive landscape now and our expectations by January, 2006.

[24] Sector made up of WAPCO and Ashaka





By 2006, we expect Lafarge which controls about 30% of present day local cement supplies through WAPCO (23%) and Ashakacem (7%), to lose its leadership position to Dangote Group, which we estimate will control about 64% of local cement supply through Obadjana (27%), Ibeshe (14%), and BCC (23%) while Lafarge controls about 23%. This paradigm is driven mainly by the proposed ban by the government of cement importation by January, 2006, which has made local manufacturers an attractive proposition to investors willing to commit funds to establishing factories in Nigeria, a country which has abundant supply of manufacturing inputs in terms of raw materials. The dividends of this transcend the local market to creating opportunities for local manufacturers on a sub-regional scale and beyond. Indeed, the Dangote group has as its long term goal, the domination of cement production and supply in the subregion. Furthermore, while some major changes are taking place in the competitive landscape locally, the market, overall, continues to experience sustained growth and the players in the industry are hardly perturbed by demand-side dynamics.

There are other changes that may benefit the industry as a whole by enhancing the local industry's manufacturing capacity. The first is the Power Sector Reform Bill which is currently at the last stages of approval in Nigeria's legislative houses, and whose implementation is expected to take off in earnest by the end of 2005. We expect the break in the stranglehold on the power sector by the National Electric Power Authority, the nation's power monopoly, to spawn an era of more efficient production and distribution of electric power by new entities. We see this improving cost and production efficiencies within the manufacturing sector, and releasing many manufactures from direct effects of supply and price fluctuation in petroleum products. The second is the ongoing reform in the banking sector which we expect to decrease borrowing costs and improve investment climate across the manufacturing sector. We note here that cost of borrowing has been the single biggest problem for WAPCO, the industry's largest producer at the moment. Many of the old problems still persist though; prime among these is inadequate infrastructure which goes beyond power supply to transportation of bulky products to far flung markets. We see this challenging the industry's sub-regional ambitions as well, unless life is breathed into utilities like the rail system. Furthermore, dependence on imports for critical machine replacements compounded by the dearth of technological capacity to service and maintain plants leaves the industry at the mercy of foreign exchange fluctuations, which often takes a negative turn, leading to price instability and increased risk of losses to extended downtime; an event the manufacturing process within the cement production industry abhors. Rising energy costs continue to be a major concern and, finally, the general weakness in the economy also poses a challenge to the industry as it portends weakness in construction activity. However, as most of the demand is driven by large scale patronage by public works, we do not see the latter affecting the industry's pricing power significantly.

Most companies within the sector have not realised profits in recent years. The only company to have done so, Ashakacem, has a comparatively competitive earnings multiple of about 9.72 relative to about 16.8 for the broader market as at end of November 2004. We, however, retain our positive outlook on the industry in the medium to long term as we expect demand to remain strong amidst the opportunities an import ban will create, and see prospects for improved earnings among cement manufacturers. Within the sector, we still maintain a positive long term view of **WAPCO**, which we view as oversold, while companies like Benue Cement Company whose fundamentals are changing rapidly may come within our watch list in the near future.

FOOD AND BEVERAGE[25]

The food and beverage sector has experienced steady growth in recent years driven largely by a growing population, higher disposable income and strong brand awareness. Notwithstanding recent growth, there remain challenges in the local business environment that continue to affect our outlook for the food and beverage sector, and the manufacturing industry as a whole. These include high energy prices as a result of recent fuel hikes, the failing infrastructure system, especially in the areas of power generation and distribution, the hazardous road networks and lack of steady water supply, which add to the operating costs of local businesses.

Despite the aforementioned concerns, our outlook for the sector remains positive. We believe the points listed below should bode well for the industry and economy as a whole. These include

- Significant capital expenditure underscoring expansionary initiatives.
- Increased marketing focus and investment in new product development.
- the ban on the importation of several goods into the country encouraged the local manufacturing industry and the production of locally produced raw materials.
- increased NAFDAC policing, clamping down on the illegal importation of banned and fake goods.
- Greater emphasis on staff training and development to improve human capital and facilitate empowerment.

The food and beverage sector outperformed the broader market, returning 24.07% over the first three quarters of 2004, compared to the 15.61% return on the NSE. The sector currently trades on a PE of 21.91x, relative to the current market average of 16.8x, reflecting strong brands and improved top line growth within the industry. Forward multiples of 20.32x (Est. market PE: 14.96x) however do not suggest much potential for earnings growth across the sector. Going forward, we believe that positive long term growth prospects, coupled with optimistic investor sentiment about the companies' strong brand names, high quality products, and dividend payout and bonus history will provide support for valuation levels. Our top pick within the sector is **Nestle Nigeria Plc**.

[25] Food and beverage sector includes 7-Up, Cadbury, Flour Mills, Nestle and Nigeria Bottling Company

Nestle has demonstrated strong top line and earnings growth, averaging 34% for turnover growth and 32% for earnings growth in the last four years. Market dominance and investments in production capacity continue to buttress an already strong liquidity position, releasing sufficient funds for working capital management as well as generous dividend payments to shareholders.

BANKING[26]

Over the year, the banking industry underwent dramatic changes marked by the new Central Bank Governor, Professor Charles Soludo's radical decision to increase the minimum capital base for commercial banks to ₦25bln (from ₦2bln) by December 2005. This development sent shock waves through the industry as most banks[27] were still grappling to meet the earlier minimum of ₦2bln. The CBN maintained its stand and implemented a phased withdrawal of public sector funds from the banking system, which led to liquidity crunch and correspondingly higher inter-bank lending rates. Though a bit abrupt, the CBN's recent moves were imperative to saving the banking sector from total collapse as the problem of gross insider abuse and credit granted under fraudulent circumstances have led to a 454% growth in non-performing loans from ₦47bln in 1994 to ₦260bln in 2003[28], accounting for 20% of the entire loans in the industry[29].

The motive of the increase in capital base was to prune the number of operational banks by promoting consolidation within the sector, thereby giving rise to bigger banks which would be able to finance long-term capital intensive projects and as a result spur growth in the real sector of the economy. In order to assist banks meet the new capital base requirement, the CBN provided incentives to promote consolidation within the industry. These incentives are:

- Authorization to deal in foreign exchange.
- Permission to take public sector deposits and recommendation to the fiscal authorities for the collection of public sector revenue.
- Prospects of managing part of Nigeria's external reserves, subject to prevailing guidelines.
- Tax incentives in the areas of capital allowances, company income tax, stamp duties, etc.
- Reduction in transaction costs with the Securities and Exchange Commission, Nigerian Stock Exchange, Corporate Affairs Commission and all other parties involved in the scheme.

In order to meet the new minimum requirement, a number of banks opted to raise funds from the capital market as big players aimed to beef up their shareholders' fund while smaller players aspired to make themselves look more attractive in a merger transaction. Consequently, there was an increase in primary market activity as banks rushed to raise funds. On the roll call were Guaranty Trust Bank (₦10.6bln), Zenith Bank (₦8bln), Oceanic Bank (₦17bln), Access Bank (₦8.7bln), Wema Bank (₦17.5bln) and Afribank (₦17bln). Other cash-needy banks resorted to private placement financing to meet their targets. Already, a few banks have begun merger and acquisition talks.

The banking sector maintained dominance in the equity market as the most active and highest capitalized sector on the Nigerian Stock Exchange. With a

[26] Sector made up of Union Bank, United Bank for Africa, First Bank, Guaranty Trust Bank and Wema Bank.
[27] As at the time of the announcement, only First Bank and Union Bank, out of the 89 operational banks in the country, had shareholders funds in excess of ₦25bln.
[28] Non Performing Loans grew 30% from ₦199bln in 2002 to ₦260bln in 2003.
[29] Source: Nigerian Deposit Insurance Cooperation 2003 Annual Report.

total sector capitalization of ₦607bln or 33% of the market index, the banking sector returned 12.19% relative to the market's 15.61% return. Trading on a current PE of 10.25x and an estimated PE of 8.99x relative to the market's current and forward multiple of 16.8x and 14.96x, valuations for the banking sector seem to remain at attractive levels. However, with the current rate of primary market activity within the sector, a gross dilution of shares would occur as a result of the public offers. This in turn would cause a reduction in earnings per share and subsequently translate into higher PE multiples thereby resulting in overvaluation across the sector, particularly in the short term. In addition, due to the large number of shares outstanding, it is going to get more difficult for banks to service their dividend and bonus payments to shareholders; both of which are major drivers of Nigerian equities.

Our analysis of developments within the industry provides a positive outlook for the banking sector in the long run, as the restructuring is likely to boost performance within the sector thereby providing an impetus for economic growth. However this evolves around the successful post-merger integration of consolidating banks. Our prognoses for the banking sector are:

- **Increased Regulation**: The CBN's current drive to enforce more strict regulations, especially in the area of insider credit, would reduce drastically, across board, the levels of non-performing loans, thereby improving the bank's financial status.
- **Larger Bank Network***:* As banks merge, we expect the newly created banks to have larger branch network coverage. Leveraging on this network, niche players can penetrate the financial service market more easily, by taking their services to markets they may not have had prior exposure to and increase the chances of pooling into the banking system the estimated over ₦400bln in the informal sector.
- **Project Finance***:* With a much larger capital and deposit base, banks can finance long-term projects in the agriculture, construction and manufacturing sectors. This is likely to promote growth within the real sector as banking shift away from foreign exchange 'round tripping' and mercantile financing. More jobs would be created and productivity would increase, thus leading to improved GDP growth.
- **Debt Market***:* Banks would have enough liquidity to participate optimally in federal and state government's short to medium term bonds. This increased participation is likely to feed into the revival of the bond market in Nigeria, and thus promote fixed income security trading.

Whilst maintaining a positive outlook for the sector, we restrict our sector picks to industry leaders; First Bank, Afribank, Zenith Bank and Guaranty Trust Bank. This is due to the level of uncertainty surrounding smaller players within the sector, who are more likely targets for mergers and acquisitions. Chief amongst our concerns is the success of the post-merger integration; we believe that given the complexity of typical merger and acquisition deals, the CBN timeframe is not sufficient for merging banks to undergo extensive due diligence and proper valuations before they come together. Also, with the extent of share dilution likely to occur as banks merge, we are of the opinion that the new banking entity cannot generate enough cash (in the short term) to match the dilution ratio. Post consolidation, the exclusive dominant players' status hitherto enjoyed by the likes of Union Bank of Nigeria, First Bank of Nigeria and United Bank for Africa, ostensibly due to their huge capitalisation, impressive asset base, high liquidity and extensive branch network, will pale significantly. This implies that, apart from age, the advantage that the old mega banks had over the so-called new generation banks has now been eroded. To the extent that these unique selling points have now become a basic requirement for the continued existence of any bank in Nigeria, these first generation banks, whose domain the new mega banks would be encroaching on, have every reason to be concerned. This view is even more relevant in view of superior service delivery, highly trained, well motivated and dynamic workforce which much younger banks have, relative to the first generation banks.

Furthermore, given the significantly higher capital base of the industry, we expect lower returns on equity across board as banks may not be able to efficiently utilise these new monies. By implication therefore, going forward, banks' earnings are unlikely to grow at the historical rate. In addition, we see less opportunity for banks to actively turnover their balance sheet, an activity which has tended to provide additional fee income. Thus, we expect the industry as a whole to command lower earnings multiple but acknowledge that technical factors may sustain the attractiveness of banks such as Zenith and Guaranty Trust.

The number and structure of the Nigerian population (estimated population of over 125mln) supports consumer banking services. Efficient customer service, people, products, target market and customer acquisition strategies are the key issues/critical success factors in consumer banking. Though the inability of the Nigerian economy to absorb large financial risks as well as lack of long term funds has inhibited consumer banking in the country, we view this as one of the growth markets for the industry in the post consolidation era. In addition, as the financial industry becomes more integrated, and banks aggressively expand branch network to increase their market share as well as penetrate other niche markets, we see public sector collection business as well as investment banking activities, as viable market segments for banks to improve fee based income.

On balance, though the sector has good long term prospects, the short/medium term outlook remains uncertain. However, to hedge investment risks in the sector, our stock picks would be restricted to banks that already have the minimum ₦25bln.

Table 7: Economic Indicators

	H1 2005e*	2004	2003	2002	2001	2000
GDP Growth	4% - 5.5%	3.5 - 5%	3.5%	3.3%	3.9%	2.8%
CPI (12-month moving average)	10-16%	18.2%(Sept)	10.8%	12.9%	18.9%	6.9%
Exchange Rate (N/$) parallel rate	136 - 145	138 - 142	130-155	134-140	120-141	118.5
MRR	14 - 16%	15% (Nov)	15.0	16.5	20.5	14.0
All-Share Index Performance	12% to 20%	15.61%**	65.8%	10.7%	35.2%	54%
All-Share Index Range	20,000-28,000	20,129 - 30,703	12,137-21,148	10,170-13,010	8,111-11,359	5,266 - 8,111

*ARM Estimates; ** As at 30 November 2004

Table 8: H2 2004 Sector Performance

Engineering Technology	10.63%	Petroleum(Marketing)	-9.06%
Agriculture	10.25%	Construction	-9.67%
Machinery (Marketing)	9.29%	Airline	-10.49%
Managed Funds	2.46%	Food/Beverages & Tobacco	-10.68%
Industrial/Domestic Products	-0.46%	Building Materials	-11.15%
Chemical & Paints	-1.34%	Automobile & Tyre	-11.76%
Footwear	-2.39%	Conglomerates	-13.88%
Computer & Office Equipment	-2.62%	Textiles	-16.80%
Insurance	-3.77%	Real Estate	-19.43%
Banking	-7.25%	Printing & Publishing	-20.42%
Healthcare	-8.09%	Breweries	-35.06%

Table 9: Best & Worst Performing Stocks

Stock	Sector	H2 2004 Return	Stock	Sector	H2 2004 Return
Eterna Oil & Gas Plc	Petroleum Marketing	415.38%	N.E.M Insurance Co (Nig) Plc	Insurance	-33.08%
Aluminium Extrusion	Industrial &	88.68%	Eko International	Banking	-35.13%
Ind.Plc	Domestic		Bank Plc		
Standard Alliance Insurance Plc	Insurance	79.61%	Wema Bank Plc	Banking	-35.89%
Crusader Insurance Plc	Insurance	72.04%	Avon Crowncaps & Container	Packaging	-37.01%
African Petroleum Plc	Petroleum Marketing	56.2%	Nigerian Brew Plc.	Breweries	-39.45%
Union Dicon Salt Plc	Food & Beverages	55.96%	IMB International Bank Plc	Banking	-39.45%
Oceanic International Bank	Banking	48.58%	Nampak Nig Plc	Packaging	-41.70%
Acen Insurance Plc	Insurance	48.00%	University Press Plc	Printing	-43.64%
WAPIC Plc	Insurance	36.90%	Gulf Bank Of Nigeria Plc	Banking	-49.52%
AIICO Insurance Plc	Insurance	36.36%	S C O A Nig. Plc	Conglome-rates	-51.74%

Table 10: Corporate Performance Scorecard

		Year End	Most recent results	Y-o-Y change in turnover	Y-o-Y change in PAT
	Banking				
1	Access Bank	31-Mar	First Quarter 04/5	19.6%	4.5%
2	Afribank	31-Mar	Third Quarter 03/4	3.0%	-27.5%
3	Chartered Bank	31-Mar	Third Quarter 03/4	15.7%	11.8%
4	FBN	31-Mar	First Quarter 04/5	12.1%	13%
5	GTB	28-Feb	Second Quarter 04/5	19.5%	18.8%
6	NAL Bank	30-Jun	Third Quarter 03/4	100.7%	123.9%
7	UBA	31-Mar	First Quarter 04/5	9.7%	6.1%
8	UBN	31-Mar	Third Quarter 03/4	13.1%	16.7%
9	Wema Bank	31-Mar	Third Quarter 03/4	32.0%	82.9%
	Breweries				
1	Guinness	30-Jun	Full Year 2003	52.3%	30.0%
2	Nigerian Breweries	31-Dec	First Quarter 04	22.4%	-21.1%
	Building materials				
1	Ashaka	31-Dec	Full Year 2003	16.7%	39.5%
2	WAPCO	31-Dec	Full Year 2003	3.5%	NA
	Conglomerates				
1	CFAO	31-Dec	Half year 2003	6.7%	9.4%
2	UAC	31-Dec	Half year 2004	12%	89.5%
3	Unilever	31-Dec	First Quarter 2004	15.5%	15.7%
	Food & beverages				
1	7-up	31-Mar	Full Year 2004	5%	-17.5%
2	Cadbury	31-Dec	Third Quarter 2004	10.3%	27.1%
3	Flour Mills	31-Mar	First Quarter 04/5	40%	22.6%
4	Nestle	31-Dec	Half year 2004	16.2%	8%
5	Nig Bottling Co.	31-Dec	Half year 2004	6.7%	-55.5%
	Petroleum Marketing				
1	AP	31-Dec	Half year 2004	79.2%	-1.5%
2	Conoil	31-Dec	Half year 2004	83.8%	26.3%
3	Mobil	31-Dec	Half year 2004	49%	262%
4	Texaco	31-Dec	Half year 2004	60%	47%
5	Total	31-Dec	Third Quarter 2004	44.9%	-1.24%
6	Oando	31-Dec	Half year 2004	62.1%	137%
	Real estate				
1	UAC properties	31-Dec	Half year 2004	39.9%	31%